90-344

No. ——

Supreme Court, U.S.
FILED
AUG 24 1990
JOSEPH F. SPANIOL, JR.
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

TRANSWESTERN PIPELINE COMPANY,
Petitioner,

v.

KANSAS POWER AND LIGHT COMPANY, *et al.*,
Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

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187

QUESTIONS PRESENTED

1. Whether the court of appeals exceeded its authority, and erred under the judicial review standards set forth in *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984), by finding that its interpretation of the judicially created "filed rate doctrine" must override the findings of the Federal Energy Regulatory Commission that the direct billing of purchased gas costs, upon termination of another mechanism for recovery of such costs, is "just and reasonable" under the standards of Section 4 of the Natural Gas Act?

2. Whether notwithstanding the Federal Energy Regulatory Commission's waiver of the "notice" requirements of Section 4 of the Natural Gas Act, the FERC's approval of the direct billing of purchased gas costs constitutes impermissible retroactive ratemaking in violation of the "filed rate doctrine"?

3. Whether the court of appeals erred in not reconciling the "filed rate doctrine" with the requirements of Section 4 of the Natural Gas Act and Section 601 of the Natural Gas Policy Act?

PARTIES TO THE PROCEEDING

In addition to Petitioner Transwestern Pipeline Company, the parties to the proceeding before the court of appeals were:

Citizens Energy Corporation
El Paso Natural Gas Company
Federal Energy Regulatory Commission
Kansas Power and Light Company
Natural Gas Clearinghouse Inc.
Pacific Gas and Electric Company
Process Gas Consumers Group
PSI, Inc.
Public Utilities Commission of the State of California
Southern California Gas Company
Southwest Gas Corporation
Texas Eastern Transmission Corporation
Williams Natural Gas Company

PETITIONER'S RULE 29.1 STATEMENT

Parent, affiliates, and subsidiaries of Petitioner:

Parent:
Enron Corp.
P.O. Box 1188
Houston, Texas 77251-1188

Subsidiaries of Enron Corporation and affiliated entities:

Belco Petroleum Corporation (Delaware)

- Belco Petroleum Corporation of Peru (Delaware)

Enron Coal Company (Delaware)
Enron Coal Pipeline Company (Delaware)
Enron Finance Corp. (Delaware)
Enron Foundation—Omaha (Nebraska)
Enron Gas Gathering, Inc. (Delaware)
Enron Gas Liquids, Inc. (Delaware)

- Enron Liquids Marketing Canada, Ltd. (Canada)
- Weddell Corporation (Liberia)

Enron Gas Marketing, Inc. (Delaware)

- Enron GasBank, Inc. (Delaware)

Enron Gas Processing Company (Delaware)

- Enron Louisiana Energy Company (Delaware)
- Enron Louisiana Transportation Company (Delaware)

Enron Gas Production Company (Texas)
Enron Gas Transportation Company (Delaware)
Enron Gas UK Limited (United Kingdom)
Enron Helium Company (Delaware)
Enron International Incorporated (Delaware)

- Enron Gas Liquids International (U.K.), Ltd. (U.K.)
- Enron Gas Liquids France S.A.R.L. (France) (Formerly NLFI France S.A.R.L.)

Enron Oil Corp. (Delaware)

- Enron Oil Limited (England)
- Enron Oil PTE Ltd. (Singapore) (Dissolution Pending)

The Protane Corporation (Delaware)

- Enron Americas Limited (Cayman Islands)
- ProCaribe Division of The Protane Corporation
- Citadel Corporation Limited (Cayman Islands)
  - Citadel Venezolana S.A. (Venezuela)
  - Industrial Gases Limited (Jamaica)
  - Manufacturera De Aparatos Domesticos, S.A. ("MADOSA") (Venezuela)
- Enron Energy Resources, Inc. (Texas)
- Industrias Ventane, S.A. (Venezuela)
  - Industrial Lacarda, S.A. (Venezuela)
  - Servicios Consolidados Ventane, S.A. (Venezuela)
  - Servicios Vengas, S.A. (Venezuela)
  - Transporte Mil Ruedas, S.A. (Venezuela)
  - Vengas de Caracas (Venezuela)
  - Vengas del Centro, S.A. (Venezuela)
  - Vengas de Occidente, S.A. (Venezuela)
  - Vengas de Oriente, S.A. (Venezuela)
- ProCaribe, Inc. (Puerto Rico)
- Progasco, Inc. (Puerto Rico)

Enron Liquid Fuels Company (Delaware)
Enron Liquids Pipeline Company (Delaware)
Enron Marketing Services, Inc. (Delaware)
Enron Minerals Company (Delaware)
Enron Mobile Bay, Inc. (Texas)
Enron NGL Corp. (Delaware)
Enron Oil & Gas Company (Delaware)—84%

Enron Exploration Company (Texas)

Enron Oil Egypt Inc. (Texas)
Enron Oil Malaysia Inc. (Texas)
Enron Oil Sumatra Ltd. (Cayman Islands)
Enron Oil Syria Inc. (Texas)

Enron Oil & Gas Marketing, Inc. (Delaware)
IN Holdings, Inc. (Delaware)

Enron Oil Canada, Ltd. (Alberta)

Enron Oil Trading & Transportation Company (Delaware)

Enron Oil Pipeline Company (A Division)
Enron Oil Trading & Transportation Canada Ltd. (Canada)

Enron U.K. Limited (United Kingdom)
Webster Transportation Company, Inc. (Louisiana)

Enron Overthrust Pipeline Company (Delaware)
Enron Power Corp. (Delaware)

Enron Power Enterprise Corp. (Delaware)
Enron Power Operating Company (Delaware)
Enron Power (U.K.) Limited (England)

Enron Products Marketing Company (Delaware)
Enron Products Pipeline, Inc. (Delaware)
Enron Property Company (Delaware)
Enron Trailblazer Pipeline Company (Delaware)
Enron Venture Capital Company (Delaware)
Falco UPG Ltd. (United Kingdom)

UPG Falco Ltd. (United Kingdom)

Gulf Company Ltd. (Bermuda)
Houston Pipe Line Company (Delaware)

Black Marlin Pipeline Company (Texas)
Coal Properties Corporation (Illinois)
Comanche Marketing, Inc. (Texas)
Cora Dock Corporation (Texas)

Enron Co-Gen Fuels Company (Texas)
Enron Gas Pipeline Operating Company (Texas)
Enron Industrial Natural Gas Company (Delaware)
Enron Interstate Pipeline Company (Delaware)
Enron Mojave, Inc. (Texas)
Enron Texoma Gas Company (Texas)
IDT Gas Supply Company (Texas)

Katy-Waha Gas Marketing Company (Texas)

Intratex Gas Company (Delaware)
Natural Gas Marketing & Storage Company (Texas)
Pacific Atlantic Marketing, Inc. (Texas)
Panhandle Gas Company (Delaware)
Riverside Farms Company (Illinois)
Transgulf Pipeline Company (Florida)
Transwestern Pipeline Company (Delaware)
Valley Pipe Lines, Inc. (Delaware)

Valley Pipe Lines Offshore Division (Assumed Name)

Webb-Duval Pipeline, Inc. (Delaware)

NGP Pipeline Company (Delaware)
Northern Intrastate Pipeline Company (Delaware)

Taft Pipeline Company (a division)

Northern Natural Gas Supply Company (Delaware)
Northern Natural Gas Company (Delaware)
Northern Plains Natural Gas Company (Delaware)

AmNorth, Inc. (Nebraska)
Northern Border Pipeline Corporation (Delaware)

Divisions of Enron Corp.

Enron EOR Services Company
Enron International Development Division
Gas Pipeline Group Division
Northern Natural Gas Company Division
San Juan Gas Company Division

Joint Venture Companies:

Border Gas, Inc. (Delaware)

Owned by Florida Gas Transmission Company—
$3\frac{1}{3}\%$

Tennessee Gas Pipeline Company—$37\frac{1}{2}\%$
Texas Eastern Transmission Corporation—
$27\frac{1}{2}\%$
El Paso Natural Gas Company—15%
Transcontinental Gas Pipe Line Corporation—
10%
Southern Natural Gas Company—$6\frac{2}{3}\%$

Citrus Corp. (Delaware)

Owned by Houston Pipe Line Company—50%
(Class B Stock)

Sonat—50% (Class A Stock)

Subsidiaries:

Citrus Industrial Sales Company, Inc.
(Delaware)
Citrus Interstate Pipeline Company (Delaware)
Citrus Marketing, Inc. (Florida)
Citrus Trading Corp. (Delaware)
Florida Gas Transmission Company (Delaware)

Enron/Dominion Cogen Corp. (Delaware)

Owned by Enron Power Corp.—50%

Dominion Resources—50%

Subsidiaries:

Enron Bayou Go-Gen, Inc. (Delaware)
Enron Cogeneration One Company (Delaware)

Cogenron Inc. (Delaware)
Owned by: ECIC 100% Common;
Outside Investors 100%
Preferred

Enron Cogeneration Three Company
(Delaware)
Enron Cogeneration Five Company
(Delaware)

Enron NGL Partners, Limited Partnership (Delaware)

Owned by Enron NGL Corp.

Subsidiaries:

Enron BTU Limited Partnership (Delaware)
Enron Helium Limited Partnership (Delaware)
Enron Liquids Pipeline Limited Partnership (Delaware)
Enron NGL Processing Limited Partnership (Delaware)

HT Gathering Company (Texas)

Owned by Houston Pipe Line Company—50% Class A Voting Common

Tenngasco—50% Class B Voting Common
Houston Pipe Line Company—100% Class B Common

Interruptores Especializados Lara, S.A. (Venezuela)

Owned by Citadel Venezolana, S.A.—66%

Terrenos Y Maquinarias Termaq, S.A.—34%

Jubilee Pipeline Company (Texas)

An Unincorporated Joint Venture among:

Enron Mobile Bay, Inc.—22.5%
Oklahoma Gas Pipeline Company—35%
Tabasco Gas Pipe Line Company—15%
Sonat Mobile Bay, Inc.—12.5%
Odeco Gas Gathering, Inc.—7.5%
Murphy Gas Gathering, Inc.—7.5%

Mojave Pipeline Operating Company (Texas)

Owned by Mojave Pipeline Company, a Partnership composed of: Enron Mojave, Inc.—50%
El Paso Mojave—50%

Norelf Limited (Bermuda)

Owned by Enron Gas Liquids, Inc.—42.5%

Corelf—42.5%
Gazocean (Bermuda) Trading Ltd.—15%

Northern Border Pipeline Company (Texas)

Owned by Northern Plains Natural Gas Company—35%

Pan Border Gas Company—22.75%
TransCanada Border PipeLine Ltd.—30%
Northwest Border Pipeline Company—12.25%

Oasis Pipe Line Company (Delaware)

Owned by Houston Pipe Line Company—25%

The Dow Chemical Co.—45%
Tenngasco Gas Supply Company—30%

Subs Oasis Pipe Line Finance Company (Delaware)

San Marco Pipeline Company (Colorado)

Owned by Houston Pipe Line Company—50%

The Denver & Rio Grande Western Railroad Co.—50%

Seagull Shoreline System (a Texas Partnership composed of

Northern Intrastate Pipeline Company—30%
Texas Eastern Offshore Company
Seagull Transmission Company)

The Standard Shale Products Company (Colorado)

Owned by Houston Pipe Line Company—30%

Conoco—70%

TABLE OF CONTENTS

	Page
OPINIONS BELOW	1
JURISDICTION	1
STATUTES INVOLVED	1
STATEMENT	2
A. Regulatory Background	2
1. Minimum Bills	2
2. PGA Clauses	2
3. Passage of the Natural Gas Policy Act	3
4. Elimination of Minimum Bills and Imposition of Open Access Requirements	4
5. FERC's Order No. 500 Series and Gas Inventory Charge Policies	7
B. Proceedings Below	8
1. Transwestern's GIC Applications	8
2. FERC's Orders and Implementation of Transwestern's GIC	10
3. The Decision Below	12
REASONS FOR GRANTING THE PETITION	16
I. THE COURT BELOW HAS IGNORED FUNDAMENTAL PRINCIPLES OF STATUTORY CONSTRUCTION	17
A. The Statutory Framework	17
B. Application of Statutory Construction Principles	17
1. FERC's Determination as to Adequacy of Notice	18
2. Waiver of Notice	22

TABLE OF CONTENTS—Continued

Page

II. CONFLICT WITH NGPA AND PGA REGULATIONS 26

III. THE D.C. CIRCUIT'S OPINION CONFLICTS WITH DECISIONS RENDERED BY OTHER FEDERAL COURTS OF APPEALS 27

CONCLUSION 30

TABLE OF AUTHORITIES

CASES Page

Arkansas Louisiana Gas Co. v. Hall, 453 U.S. 571 (1981) 17, 18, 22
Associated Gas Distributors v. FERC, 824 F.2d 981 (D.C. Cir. 1987), *cert. denied sub nom. Interstate Natural Gas Ass'n v. FERC*, 485 U.S. 1006 (1988) 6, 7
Associated Gas Distributors v. FERC, 893 F.2d 349 (D.C. Cir. 1989), petitions for cert. filed, 59 U.S.L.W. 3001 (U.S. June 20, 1990) (No. 89-1988), 59 U.S.L.W. 3001 (U.S. June 21, 1990) (Nos. 89-1989, 89-1990), 59 U.S.L.W. 3001 (U.S. June 22, 1990) (No. 89-2000), and 59 U.S.L.W. 3005 (U.S. June 21, 1990) (No. 89-2016) 8, 13, 29
Chevron U.S.A. Inc. v. NRDC, Inc., 467 U.S. 837 (1984) 17-20, 25
City of Piqua v. FERC, 610 F.2d 950 (D.C. Cir. 1979) 24, 25, 30
City of Willcox v. FPC, 567 F.2d 394 (D.C. Cir. 1977), *cert. denied*, 434 U.S. 1012 (1978) 22
Columbia Gas Transmission Corp. v. FERC, 895 F.2d 791 (D.C. Cir. 1990), petitions for cert. filed, 59 U.S.L.W. 3005 (U.S. June 22, 1990) (No. 89-2001), 59 U.S.L.W. 3066 (U.S. July 18, 1990) (No. 90-131) ..... *passim*
Columbia Gas Transmission Corp. v. FERC, 844 F.2d 879 (D.C. Cir. 1988) 11
Columbia Gas Transmission Corp. v. FERC, 831 F.2d 1135 (D.C. Cir. 1987) 13
Electric District No. 1 v. FERC, 774 F.2d 490 (D.C. Cir. 1985) 14
FPC v. Hope Natural Gas Co., 320 U.S. 591 (1944) 17, 18, 20
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K Mart Corp. v. Cartier, Inc., 486 U.S. 281 (1988) .. 18
Phillips Petroleum Co. v. FERC, 902 F.2d 795 (10th Cir. 1990) 27-30
Public Service Company of New Hampshire v. FERC, 600 F.2d 944 (D.C. Cir. 1979), *cert. denied*, 444 U.S. 990 (1979) ..... *passim*

TABLE OF AUTHORITIES—Continued

Page

Shell Oil Co. v. FERC, 566 F.2d 536 (5th Cir. 1978), *aff'd*, 440 U.S. 192 (1979) 22
Texas Eastern Transmission Corp. v. FERC, 768 F.2d 1053 (5th Cir. 1985), *cert. denied sub nom. Associated Gas Distributors v. FERC*, 476 U.S. 1114 (1986) 27-30
Towns of Concord and Wellesley v. FERC, 844 F.2d 891 (1st Cir. 1988) 26
Transwestern Pipeline Co. v. FERC, 897 F.2d 570 (D.C. Cir. 1990) ..... *passim*
United Gas Pipe Line Co. v. FPC, 385 U.S. 83 (1966) 9
Water Transport Ass'n v. ICC, 715 F.2d 581 (D.C. Cir. 1983), *cert. denied*, 465 U.S. 1006 (1984) 22

STATUTES

Natural Gas Act of 1938,
15 U.S.C. §§ 717, *et seq.* ..... *passim*
15 U.S.C. § 717c ..... *passim*
15 U.S.C. § 717d 16, 22, 26
15 U.S.C. § 717f ..... *passim*
Natural Gas Policy Act of 1978,
15 U.S.C. §§ 3301, *et seq.* ..... *passim*
15 U.S.C. § 3320 ..... 27, 28
15 U.S.C. § 3431 ..... *passim*

ADMINISTRATIVE

Compression Allowances and Protest Procedures Under NGPA Section 110, Order No. 473, FERC Stats. & Regs. [Regulations Preambles] ¶ 30,747 (1987), *modified*, Order No. 473-A, FERC Stats. & Regs. [Regulations Preambles] ¶ 30,788 (1988) 28-29
Elimination of Variable Costs from Certain Natural Gas Pipeline Minimum Commodity Bill Provisions, Order No. 380, FERC Stats. & Regs. [Regulations Preambles 1982-85] ¶ 30,571, *clarified and stayed in part*, Order No. 380-A, FERC

TABLE OF AUTHORITIES—Continued

Page

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Purchased Gas Cost Adjustment Provision in Natural Gas Pipeline Companies' FPC Gas Tariffs, Order No. 452, 47 F.P.C. 1049 *modified,* 47 F.P.C. 1510 (1972), *modified,* 49 F.P.C. 84 (1973) 3

Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol, Order No. 436, FERC Stats. & Reg. [Regulations Preambles 1982-85] ¶ 30,665, *modified,* Order No. 436-A, FERC Stats. & Regs. [Regulations Preambles 1982-85] ¶ 30,675 (1985), *modified further,* Order No. 436-B, FERC Stats. & Regs. [Regulations Preambles] ¶ 30,688, *reh'g denied,* Order No. 436-C, 34 F.E.R.C. ¶ 61,404, *reh'g denied,* Order No. 436-D, 34 F.E.R.C. ¶ 61,405, *reconsideration denied,* Order No. 436-E, 34 F.E.R.C. ¶ 61,403 (1986), *vacated and remanded sub nom. Associated Gas Distributors v. FERC,* 824 F.2d 981 (D.C. Cir. 1987), *cert. denied sub nom. Interstate Natural Gas Ass'n of America v. FERC,* 485 U.S. 1006 (1988) 6, 30

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TABLE OF AUTHORITIES—Continued

Page

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Sales and Transportation by Interstate Pipelines and Distributors; Expansion of Categories of Activities Authorized Under Blanket Certificate, Order No. 319, FERC Stats. & Regs. [Regulations Preambles 1982-85] ¶ 30,477, *modified,* Order No. 319-A, FERC Stats. & Regs. [Regulations Preambles 1982-85] ¶ 30,511 (1983) 5

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Transwestern Pipeline Company,

41 F.E.R.C. ¶ 61,371 (1987) 10
42 F.E.R.C. ¶ 61,370 (1988) 10
43 F.E.R.C. ¶ 61,240 (1988) 10, 12
44 F.E.R.C. ¶ 61,164 (1988) 10-12, 23
48 F.E.R.C. ¶ 61,136 (1989) 12
49 F.E.R.C. ¶ 61,350 (1989) 12
49 F.E.R.C. ¶ 61,436 (1989) 12
50 F.E.R.C. ¶ 61,427 (1990) 12

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

Transwestern Pipeline Company ("Transwestern") hereby petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the District of Columbia Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals is reported at 897 F.2d 570 (D.C. Cir. 1990) and appears at pages 1a-25a of the Appendix. The orders denying rehearing and denying suggestions for rehearing *en banc*, together with the separate statement of Chief Judge Wald, are unpublished but are reproduced in the Appendix at pages 26a-28a.

The relevant orders of the Federal Energy Regulatory Commission ("Commission" or "FERC") are reported at 41 F.E.R.C. ¶ 61,371 (1987) (App. 30a-39a), 42 F.E.R.C. ¶ 61,370 (1988) (App. 40a-54a), 43 F.E.R.C. ¶ 61,240 (1988) (App. 55a-98a) and 44 F.E.R.C. ¶ 61,164 (1988) (App. 99a-127a).

JURISDICTION

The judgment of the court of appeals was entered on March 23, 1990. App. 1a-25a. Rehearing was denied on May 31, 1990. App. 26a. This Court has jurisdiction under 28 U.S.C. § 1254(1). The court of appeals granted a stay of its mandate on June 27, 1990 pending the filing, by August 27, 1990, of a petition for a writ of certiorari. App. 29a.

STATUTES INVOLVED

Sections 4, 5 and 7 of the Natural Gas Act of 1938, 15 U.S.C. §§ 717c, 717d and 717f, and Section 601 of the Natural Gas Policy Act of 1978, 15 U.S.C. § 3431, are reproduced in the Appendix at 128a-140a.

STATEMENT

A. *Regulatory Background*

1. Minimum Bills

In their historical role as natural gas merchants, interstate pipelines purchased natural gas from producers and then transported and resold the gas to their customers—primarily local distribution companies, other interstate pipelines and end-users. Prior to 1978 the prices received by the producers for these sales were subject to Natural Gas Act ("NGA") [1] regulation by FERC; and all sale for resale rates charged by interstate pipelines are subject to comprehensive FERC regulation under the NGA, as are the terms of service between these pipelines and their customers.

In order to perform their sale for resale services, interstate pipelines entered into long term contracts with producers. These contracts contained "take-or-pay" clauses that required the pipelines to take a certain amount of gas, or pay for that amount of gas if it was not taken. In turn, the pipelines included, in their FERC tariffs, minimum bill provisions which obligated their customers to pay at least certain of the pipelines' variable costs, including the costs of gas purchased by the pipelines whether or not the customers actually purchased any gas. The minimum bill provisions ensured that pipelines would be able to recover their gas costs and avoid or minimize their accrual of take-or-pay liability.

2. PGA Clauses

Prior to 1972, interstate pipelines traditionally recovered increases in gas costs charged to them by their producer-suppliers through general rate filings made pursuant to Section 4 of the NGA, 15 U.S.C. § 717c. As wellhead prices began to escalate more rapidly, pipelines were required to make NGA Section 4 general rate filings with greater frequency. In order to "permit pipeline com-

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[1] 15 U.S.C. §§ 717, *et seq.*

panies to protect themselves against supplier rate increases without frequent general [Section 4] rate increase applications," the Commission promulgated regulations providing for the establishment of the purchased gas adjustment ("PGA") clause, which enabled pipelines to automatically track and recover gas acquisition costs.[2] Under the typical PGA clause, the pipeline estimates the volumes of gas to be purchased, estimates the prices of such purchases for a six month period, and implements rates based upon these estimates through semi-annual NGA Section 4 filings with FERC.[3] Because the PGA clause is an estimation process, undercollections or overcollections almost always occur. Therefore, the Commission provided that all overcollections or undercollections were to be booked into an account, referred to as Account No. 191. Pipelines were then required to amortize any balances in Account No. 191 and, in their next NGA Section 4 PGA filing, refund or surcharge to their customers the overcollections or undercollections, as appropriate. The Commission designed this mechanism to "assure the recovery of all purchased gas costs" by the pipeline, as well as keep its customers whole.[4] Thus, PGA clauses operated in tandem with minimum bill provisions to provide pipelines with the ability to recover all costs associated with acquiring and maintaining supplies under gas purchase contracts necessary to meet the pipelines' sales obligations.

3. Passage of the Natural Gas Policy Act

In the 1970's, interstate pipelines began experiencing gas supply shortages brought about by the disparity in

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[2] *Purchased Gas Cost Adjustment Provision in Natural Gas Pipeline Companies' FPC Gas Tariffs*, Order No. 452, 47 F.P.C. 1049, 1050, *modified*, 47 F.P.C. 1510 (1972), *modified*, 49 F.P.C. 84 (1973).

[3] In 1987, FERC modified its regulations governing the PGA mechanism to require that pipe lines file one comprehensive annual PGA filing, instead of two semi-annual filings, and then update the annual filing quarterly. *See Revisions to the Purchased Gas Adjustment Regulations*, Order No. 483, FERC Stats. & Regs. [Regulations Preambles] ¶ 30,778 (1987).

[4] 47 F.P.C. at 1053.

prices that existed between the intrastate and interstate natural gas markets. In an attempt to remedy these shortages and to allow competitive market forces to have greater influence on the natural gas industry, Congress enacted the Natural Gas Policy Act of 1978 ("NGPA"), 15 U.S.C. §§ 3301, *et seq.* Although FERC's authority under the NGA to regulate the rates, charges and terms of sales for resale services between interstate pipelines and their customers was undisturbed by the NGPA, the setting of wellhead prices was removed from FERC's regulation. The NGPA established price ceilings for various categories of natural gas and provided for phased deregulation of certain other categories of gas. In addition, the NGPA exempted from FERC's NGA jurisdiction the transportation of gas by interstate pipelines on behalf of local distribution companies. This gave these distribution companies the option of purchasing gas directly at the wellhead, with transportation performed by the pipelines under the NGPA. Finally, the NGPA guaranteed interstate pipelines the right to recover all purchased gas costs absent a showing of fraud or abuse. *See* 15 U.S.C. § 3431(c)(2).[5]

4. Elimination of Minimum Bills and Imposition of Open Access Requirements

In the early 1980's, demand for natural gas decreased due to the economic recession, warmer weather, and fuel switching which resulted from the steep decline in oil

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[5] Section 601(b) and (c), 15 U.S.C. §§ 3431 (b) and (c), provide in pertinent part

> (b) for purposes of sections 4 and 5 of the Natural Gas Act, any amount paid in any first sale of natural gas shall be deemed to be just and reasonable if (i) such amount does not exceed the applicable maximum lawful price. . . .
>
> (c) [f]or purposes of sections 4 and 5 of the Natural Gas Act, the Commission may not deny any interstate pipelines recovery of any amount paid with respect to any purchase of natural gas if, under subsection (b) of this section, such amount is deemed to be just and reasonable . . . except to the extent the Commission determines that the amount paid was excessive due to fraud, abuse, or similar grounds.

prices. At the same time, there occurred a substantial increase in supplies resulting from the NGPA's natural gas price incentives and phased deregulation. Because the supply of natural gas exceeded demand, interstate pipelines could not sell gas they were otherwise obligated to purchase under long term fixed price contracts, most of which contained take-or-pay provisions and which were entered into during the time of natural gas shortages. Therefore, the pipelines began to accrue substantial take-or-pay liability; and, cheap supplies of gas remained available in the so-called "spot" market.

To provide local distribution companies and end-users with greater access to these "spot" market supplies, the FERC in 1983 simplified the requirements necessary for transportation services performed by interstate pipelines.[6] In part because pipelines would lack incentive to perform NGPA and NGA transportation services if the gas transported would displace sales of gas by the pipeline under contracts containing take-or-pay clauses, FERC, in 1984, issued Order No. 380.[7] This order required interstate pipelines to eliminate gas costs from the minimum bill provisions of their tariffs. FERC subsequently, on a case-by-case basis, eliminated minimum bills altogether.[8]

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[6] *Sales and Transportation by Interstate Pipelines and Distributors; Expansion of Categories of Activities Authorized Under Blanket Certificate*, Order No. 319, FERC Stats. & Regs. [Regulations Preambles 1982-85] ¶ 30,477, *modified*, Order No. 319-A, FERC Stats. & Regs. [Regulations Preambles 1982-85] ¶ 30,512 (1983).

[7] *Elimination of Variable Costs from Certain Natural Gas Pipeline Minimum Commodity Bill Provisions*, Order No. 380, FERC Stats. & Regs. [Regulations Preambles 1982-85] ¶ 30,571, at 30,963, *clarified and stayed in part*, Order No. 380-A, FERC Stats. & Regs. [Regulations Preambles 1982-85] ¶ 30,584, *reh'g denied*, Order No. 380-B, 29 F.E.R.C. ¶ 61,076, *aff'd and stay lifted*, Order No. 380-C, FERC Stats. & Regs. [Regulations Preambles 1982-85] ¶ 30,607, *reh'g denied*, Order No. 380-D, 29 F.E.R.C. ¶ 61,332 (1984), *aff'd in pertinent part sub nom. Wisconsin Gas Co. v. FERC*, 770 F.2d 1144 (D.C. Cir. 1985), *cert. denied sub nom. Transwestern Pipeline Co. v. FERC*, 476 U.S. 1114 (1986).

[8] *See, e.g., Transwestern Pipeline Company*, 32 F.E.R.C. ¶ 61,009 (1985), *reh'g denied*, 36 F.E.R.C. ¶ 61,175 (1986), *aff'd, Transwest-*

FERC reasoned that elimination of minimum bills would enhance competition between "spot" gas available for purchase directly by end-users and local distribution companies, and gas available for sale by the pipelines. Yet, while FERC eliminated all minimum bills, it did not alter the pipelines' sales service obligations to their customers or the pipelines' take-or-pay obligations to their producer-suppliers. Therefore, pipelines were required to continue to stand ready to meet FERC-approved sales service obligations, with no assurance that customers would continue to purchase any supplies from the pipeline and with no escape from the resulting take-or-pay exposure.

In Order No. 436,[9] FERC undertook a "complete restructuring of the natural gas industry." *Associated Gas Distributors v. FERC*, 824 F.2d 981, 993 (D.C. Cir. 1987), *cert. denied sub nom. Interstate Natural Gas Ass'n of America v. FERC*, 485 U.S. 1006 (1988). Order No. 436 introduced "open access" as an integral feature of the Commission's regulatory policies for interstate pipelines, under which pipelines were required to transport gas on a nondiscriminatory basis, even if such transportation would displace the pipeline's own sales.

As a result of the above described initiatives, FERC provided end-users and local distribution companies total flexibility to choose among a variety of service options—primarily purchases of cheap "spot" gas directly at the wellhead with essentially mandatory transportation by

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ern Pipeline Co. v. FERC, 820 F.2d 733 (5th Cir. 1987), *cert. denied*, 484 U.S. 1005 (1988).

[9] *Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, Order No. 436, FERC Stats. & Regs. [Regulations Preambles 1982-85] ¶ 30,665, *modified*, Order No. 436-A, FERC Stats. & Regs. [Regulations Preambles 1982-85] ¶ 30,675 (1985), *modified further*, Order No. 436-B, FERC Stats. & Regs. [Regulations Preambles] ¶ 30,688, *reh'g denied*, Order No. 436-C, 34 F.E.R.C. ¶ 61,404, *reh'g denied*, Order No. 436-D, 34 F.E.R.C. ¶ 61,405, *reconsideration denied*, Order No. 436-E, 34 F.E.R.C. ¶ 61,403 (1986), *vacated and remanded sub nom. Associated Gas Distributors v. FERC*, 824 F.2d 981 (D.C. Cir. 1987), *cert. denied sub nom. Interstate Natural Gas Ass'n of America v. FERC*, 485 U.S. 1006 (1988).

the pipeline or purchases from the pipeline. At the same time, however, FERC did not require customers to reduce their contract demand entitlements in their gas sales contracts with pipelines, nor did FERC eliminate a pipeline's obligation to maintain a level of supplies sufficient to serve the contract demand levels of its customers. Thus, the take-or-pay exposure of pipelines grew enormously. In addition, the level of unrecovered gas costs—and, therefore, the Account No. 191 surcharges—also grew enormously, in part, because of an ever-increasing reliance by the pipelines' customers on cheaper "spot" supplies in lieu of purchases from the pipeline.

5. FERC's Order No. 500 Series and Gas Inventory Charge Policies

FERC's initiatives in Order No. 436 were reversed and remanded in *Associated Gas Distributors v. FERC*, 824 F.2d 981 (D.C. Cir. 1987), *cert. denied sub nom. Interstate Natural Gas Ass'n of America v. FERC*, 485 U.S. 1006 (1988) (*"AGD I"*). The court directed that, on remand, the Commission "must more convincingly address the magnitude of the [take-or-pay] problem and the adverse consequences likely to result from the non-discriminatory access . . . conditions." 824 F.2d at 1044. In response to *AGD I*, FERC issued Order No. 500,[10] which established a two-pronged approach to deal with the take-or-pay problem. The first mechanism was designed to deal with existing take-or-pay liability. Under this "equitable sharing" mechanism, a pipeline was per-

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[10] *Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, Order No. 500, FERC Stats. & Regs. ¶ 30,761, *modified*, Order No. 500-A, FERC Stats. & Regs. ¶ 30,770, *reh'g granted in part*, Order No. 500-B, FERC Stats. & Regs. ¶ 30,772, *modified*, Order No. 500-C, FERC Stats. & Regs. ¶ 30,786 (1987), *modified*, Order No. 500-D, FERC Stats. & Regs. ¶ 30,800, *reh'g denied*, Order No. 500-E, 43 F.E.R.C. ¶ 61,234, *modified*, Order No. 500-F, FERC Stats. & Regs. ¶ 30,841 (1988), *reh'g denied*, Order No. 500-G, 46 F.E.R.C. ¶ 61,148 (1989), *remanded sub nom. American Gas Ass'n v. FERC*, 888 F.2d 136 (D.C. Cir. 1989), *order on remand*, Order No. 500-H, FERC Stats. & Regs. ¶ 30,867 (1989), *reh'g denied in part*, Order No. 500-I, FERC Stats. & Regs. ¶ 30,880 (1990).

mitted to direct bill its customers for up to one-half of its take-or-pay, buy-out, buy-down and contract reformation costs, provided it agreed to absorb an equal amount of such costs.[11] The second mechanism, designed to prevent future accrual of take-or-pay costs, allowed a pipeline to "include in its tariff a charge, not related to facilities, for standing ready to supply gas to sales customers."[12] This second mechanism, or Gas Inventory Charge ("GIC"), was to serve as an alternative to both the PGA mechanism and the minimum commodity bill by compensating pipelines "for contracting for a gas supply to meet its customers' requirements."[13] FERC envisioned that the GIC would "help pipelines restructure their service obligations to customers and their purchase obligations to producers so as to reflect the realities of anticipated future operations and prevent future take-or-pay problems."[14]

B. *Proceedings Below*

1. Transwestern's GIC Applications

On December 1, 1987, Transwestern submitted a comprehensive proposal under Sections 4 and 7 of the NGA, 15 U.S.C. §§ 717c, 717f, to implement a GIC. The tariff sheets filed by Transwestern under Section 4 of the NGA provided that Transwestern's two jurisdictional sales customers—Southern California Gas Company ("SoCal")

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[11] The amounts each customer owed was based on its reduction in purchases, or "purchase deficiency," as compared to that customer's purchases during the period preceding the pipeline's accrual of significant take-or-pay exposure. The D.C. Circuit struck down this methodology, holding that it violated the filed rate doctrine in *Associated Gas Distributors v. FERC*, 393 F.2d 349 (D.C. Cir. 1989), petitions for cert. filed, 59 U.S.L.W. 3001 (U.S. June 20, 1990) (No. 89-1988), 59 U.S.L.W. 3001 (U.S. June 21, 1990) (Nos. 89-1989 and 89-1990), 59 U.S.L.W. 3001 (U.S. June 22, 1990) (No. 89-2000), and 59 U.S.L.W. 3005 (U.S. June 21, 1990) (No. 89-2016) (*"AGD II"*).

[12] Order No. 500, FERC Stats. & Regs. [Regulations Preambles] ¶ 30,761 at 30,792 (1987).

[13] *Id.* at 30,793.

[14] *Id.*

and Williams Natural Gas Company ("Williams")—would be permitted to nominate a level of sales service within their existing contract demand levels, based upon Transwestern's posted gas prices and GIC rates (which were designed to recover the cost of currently reserving gas supplies). Transwestern also requested NGA Section 7 authority for the abandonment of sales service rights and obligations by and between Transwestern, and SoCal and Williams to the extent such services exceeded the customer's nominations under the GIC procedures.[15] In addition, Transwestern proposed that each customer's NGA certificated sales entitlement[16] be converted to an entitlement to firm transportation service to the extent such capacity was not nominated for firm sales service.

An integral feature of Transwestern's GIC proposal was the termination of Transwestern's PGA clause, and the direct billing of any undercollections or the refunding of any overcollections remaining in Account No. 191 for gas acquisition costs incurred by Transwestern prior to implementation of the GIC and termination of the PGA clause. Transwestern proposed that the direct bills or refunds be based upon each customer's then existing sales contract entitlement, and that the refunds be made or direct bills rendered after termination of the PGA mechanism. As Transwestern explained in its December 1, 1987 filing, clearing Account No. 191 was a necessary prerequisite to the rights given to Transwestern's customers to convert their purchase rights to transportation rights, or to abandon their purchase rights altogether.

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[15] Section 7(b) of the NGA, 15 U.S.C. § 717f(b), provides in part that "No natural-gas company shall abandon . . . any service . . . without the permission and approval of the Commission first had and obtained. . . ." The requirements of Section 7(b) apply to both the sales rights and obligations as well as the rights and obligations with respect to purchases of natural gas. *See United Gas Pipe Line Co. v. FPC*, 385 U.S. 83 (1966).

[16] These entitlements were established initially by contract between Transwestern and each customer, and were subsequently certificated by FERC in accordance with the requirements of Section 7(c) of the NGA, 15 U.S.C. § 717f(c).

Transwestern stated that if Account No. 191 was not cleared as a part of the requested NGA Section 7(b) authorization, Transwestern would be exposed to undercollections by virtue of the termination of its PGA clause.[17]

2. FERC's Orders and Implementation of Transwestern's GIC

Instead of allowing Transwestern's GIC proposal to become effective, or suspending the proposal for the maximum period allowed by Section 4 of the NGA,[18] FERC rejected the Section 4 filing and redocketed Transwestern's GIC proposal under Section 7 of the NGA.[19] FERC's action was based upon its belief that Transwestern's proposal resulted in a fundamental change in the service relationships between Transwestern and its customers which warranted review under the standards of Section 7 of the NGA.[20]

By orders issued May 11 and July 29, 1988, FERC approved Transwestern's GIC proposal under Sections 7(b) and 7(c) of the NGA.[21] By these orders, FERC also permitted Transwestern, upon termination of its PGA clause, to direct bill its customers for any "unrecovered Account No. 191 costs actually paid or incurred . . . ."[22]

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[17] In fact, upon implementation of the GIC, SoCal exercised its rights under the Commission's NGA Section 7 authorizations to fully convert to transportation and Williams exercised its right to leave the system entirely.

[18] Section 4(e) of the NGA, 15 U.S.C. § 717c(e), permits the FERC to suspend the operation of a "rate, charge, classification, or service, but not for a longer period than five months. . . ."

[19] *See, Transwestern Pipeline Company*, 41 F.E.R.C. ¶ 61,371 (1987), *reh'g denied*, 42 F.E.R.C. ¶ 61,370 (1988), App. 30a-54a.

[20] 41 F.E.R.C. at 62,006, App. 35a.

[21] *See Transwestern Pipeline Company*, 43 F.E.R.C. ¶ 61,240 and 44 F.E.R.C. ¶ 61,164 (1988), App. 55a-127a.

[22] 44 F.E.R.C. at 61,537, App. 118a. FERC provided that both of Transwestern's customers could challenge the prudence and reasonableness of any amounts sought to be directly billed by Transwestern. *Id.* at 61,538, App. 114a.

FERC found that "[t]o require Transwestern to absorb potential undercollections related to gas purchases made before implementation of the GIC would be unreasonable because there is no showing that the costs at issue have been imprudently or abusively incurred." [23] FERC also rejected arguments that direct billing constitutes retroactive ratemaking, stating that

> Transwestern's customers had adequate notice that they would pay Transwestern's actual gas costs through operation of the surcharge component of the PGA mechanism. . . . Direct billing serves as an appropriate surrogate for recovery through the surcharge component. Moreover, even if the Commission were to accept, *arguendo*, that direct billing of possible undercollections constitutes retroactive ratemaking, the Commission has power to waive the filed rate doctrine [citing *Columbia Gas Transmission Corp. v. FERC*, 844 F.2d 879, 880 (D.C. Cir. 1988)]. The circumstances in this case would warrant exercise of that waiver power, assuming that any waiver is necessary, for use of direct billing as a transitional mechanism which aligns cost recovery to cost causation.

44 F.E.R.C. at 61,537, App. 113a.

The "adequate notice" referred to by FERC consisted of its PGA regulations and Transwestern's semi-annual NGA Section 4 PGA filings, which were made in accordance with the express terms of Transwestern's tariff on file with FERC. These filings reflected the total gas acquisition costs which Transwestern had incurred but had not as yet recovered and which, therefore, had accumulated in Account No. 191. These filings also included the individual surcharge component of each new sales rate, which was an estimated charge designed to recover all previously unrecovered gas costs booked into Account No. 191 based upon estimated future sales.

On June 30, 1989, Transwestern filed tariff sheets to implement the GIC mechanism, and terminated its PGA

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[23] *Id.* at 61,537, App. 112a.

mechanism on September 30, 1989. In accordance with FERC's orders, Transwestern filed tariff sheets, on November 30, 1989 and February 28, 1990, under Section 4 of the NGA to direct bill all unrecovered purchased gas costs paid by Transwestern to its producer-suppliers for sales services rendered by Transwestern to SoCal and Williams for periods prior to October 1, 1989.[24]

3. The Decision Below

Transwestern, the Public Utilities Commission of the State of California ("CPUC") and Kansas Power and Light Company ("KP&L") sought judicial review of the FERC's orders before the United States Court of Appeals for the District of Columbia Circuit. Transwestern challenged, among other things, the Commission's action in redocketing Transwestern's NGA Section 4 filing under Section 7 of that Act. KP&L and the CPUC appealed, among other things, the GIC mechanism itself and the Commission's authorization to direct bill any remaining Account No. 191 balances.

On March 23, 1990, the D.C. Circuit rendered the opinion that is the subject of this petition for writ of certiorari. *See Transwestern Pipeline Co. v. FERC*, 897 F.2d 570 (D.C. Cir. 1990), App. 1a-25a. In that decision, the court held that many of the challenges to the Commission orders under review had been rendered moot as a result of SoCal's and Williams' election to nominate zero volumes for sales service under the GIC mechanism.[25] The court did, however, review the challenge to the direct billing of the Account No. 191 balance.

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[24] These filings were accepted and made effective, subject to refund and further review by FERC. *See Transwestern Pipeline Company*, 43 F.E.R.C. ¶ 61,240 (1988), 44 F.E.R.C. ¶ 61,164 (1988), 48 F.E.R.C. ¶ 61,136 (1989), 49 F.E.R.C. 61,350 (1989), 49 F.E.R.C. ¶ 61,436 (1989), and 50 F.E.R.C. ¶ 61,427 (1990).

[25] The court found that Transwestern's challenge to the Commission's action in rejecting Transwestern's Section 4 filing and redocketing it under NGA Section 7 (which had the effect of delaying collection of the rates) was moot because the rates would not have

The court found that the direct billing by Transwestern of any PGA Account No. 191 balances remaining at the time of termination of the PGA clause and which had accrued before May 11, 1988—the date on which FERC issued to Transwestern its GIC certificate and, therefore, in the court's view, the date on which Transwestern's customers were first on notice that they would be charged previously unrecovered purchased gas costs—would constitute impermissible retroactive ratemaking, in violation of the "filed rate doctrine." [26] The court defined the "filed rate doctrine" as one which

> prohibits the Commission from imposing a rate different from the one on file at the time gas is sold. . . . It allows purchasers of gas to know in advance the consequences of purchasing decisions they make, *see Columbia Gas Transmission Corp. v. FERC*, 831 F.2d 1135, 1141 (D.C. Cir. 1987). . . .

897 F.2d at 577, App. 14a-15a. While the court found that the "filed rate doctrine" requires that notice of a change in rates be provided,[27] the court also found that FERC had no power to waive the notice requirements altogether, citing *Columbia Gas Transmission Corp. v. FERC*, 895 F.2d 791 (D.C. Cir. 1990), petitions for cert. filed, 59 U.S.L.W. 3005 (U.S. June 22, 1990) (No. 89-

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been assessed anyway. In addition, the court found that KP&L's and CPUC's attacks on the GIC mechanism itself were moot because the GIC would never be assessed.

[26] In reaching this conclusion the court applied essentially the same interpretation of the filed rate doctrine and retroactive ratemaking as it had in *Columbia Gas Transmission Corp. v. FERC*, 895 F.2d 791 (D.C. Cir. 1990), petitions for cert. filed, 59 U.S.L.W. 3005 (U.S. June 22, 1990) (No. 89-2001) and 59 U.S.L.W. 3066 (U.S. July 18, 1990) (No. 90-131) and *AGD II*.

[27] Section 4(d) of the NGA, 15 U.S.C. § 717c(d), provides that "[u]nless the Commission otherwise orders, no change shall be made by any natural-gas company in any such rate, charge, classification, or service, or in any rule, regulation or contract relating thereto, except after thirty days' notice to the Commission and to the public. . . . The Commission, for good cause shown, may allow changes to take effect without requiring the thirty days' notice. . . ."

2001) and 59 U.S.L.W. 3066 (U.S. July 18, 1990) (No. 90-131) (*"Columbia II"*). 897 F.2d at 580, App. 21a.

In analyzing what constitutes adequate notice to satisfy its view of the "filed rate doctrine," the court recognized that "[o]ur decisions on the necessary notice have not been altogether clear." 897 F.2d at 577, App. 15a. The court then compared its decision in *Electric District No. 1 v. FERC*, 774 F.2d 490 (D.C. Cir. 1985), which the court admitted adopted a "bright-line insistence that a numerical rate be 'specified,'" 897 F.2d at 577, App. 15a, with its decision in *Public Service Co. of New Hampshire v. FERC*, 600 F.2d 944 (D.C. Cir.), *cert denied*, 444 U.S. 990 (1979) (*"Public Service"*), where the court concluded that "the rule against retroactive ratemaking would be no bar to collection of [costs leftover as a result of a transition from one billing system to another]." 897 F.2d at 578, App. 16a. The court then determined that the better of the two inconsistent interpretations was one which would not require identification of a specific numerical rate; that FERC "need not confine rates to specific, absolute numbers but may approve a tariff containing a rate 'formula' or a rate 'rule' . . . ." 897 F.2d at 578, App. 16a. The court then summarized its attempted reconciliation stating that

> [i]n so far as prior discussions in our cases have suggested that a rate violates the filed rate doctrine simply because a customer cannot respond in some way that enables it to escape the charge, such remarks were clearly inconsistent with the acknowledged power of the Commission to establish, and to alter prospectively, fixed charges . . . . avoidable if at all only through the elaborate process of securing abandonment under § 7 of the Act.

897 F.2d at 579 (citations omitted), App. 19a.

After enunciating these principles—that the rule against retroactive ratemaking does not bar collection of costs resulting from changes in billing systems, that notice of a specific numerical rate is not necessary, that notice of a rate formula (*e.g.* the surcharge component

of a PGA clause or a direct bill mechanism) is permissible and that FERC could alter prospectively fixed charges which a customer must pay absent a NGA Section 7 grant of unconditional abandonment authority—the court inexplicably found that Transwestern's customers had "no meaningful notice" prior to May 11, 1988 (the date of the Commission's order approving the GIC certificate) of the direct billing of Account No. 191 balances. The court rejected arguments that adequate notice was provided through (1) promulgation of the PGA regulations; (2) operation of the surcharge component of the PGA mechanism—which informed each of Transwestern's affected customers, through semi-annual NGA Section 4 filings, of the Account No. 191 balances yet to be refunded (overcollections) or recovered (undercollections); (3) operation of Transwestern's tariff, which authorized collections of Account No. 191 surcharges; (4) a series of 1986 FERC cases permitting the direct billing of unrecovered Account No. 191 costs upon the termination of PGA clauses; or (5) Transwestern's December 1, 1987 filing itself which proposed the direct billing or refunding of Account No. 191 balances.

Transwestern and FERC filed petitions for rehearing and suggestions for rehearing *en banc* of the court's opinion. Both argued that the court erred in holding that Transwestern's customers had no meaningful notice prior to May 11, 1988. In their petitions for rehearing, FERC and Transwestern pointed out that Transwestern's customers were on notice—as early as 1972 with the promulgation of the PGA regulations themselves, and no later than December 1, 1987, the date of Transwestern's NGA Section 4 filing—that they would be responsible for all Account No. 191 balances upon termination of the PGA mechanism. On May 31, 1990, the court denied rehearing and denied the suggestions for rehearing *en banc*. By separate statement (App. 29a), Chief Judge Wald expressed her concern for the court's "overly rigid" interpretation of the "filed rate doctrine" "at a time when the FERC needs latitude to navigate the recent dramatic

changes in the structure of the natural gas industry", and noted the significance of the court's ruling with regard to the notice issue by stating

> [i]t remains for the Supreme Court to settle this important question of how impenetrable a barrier the filed rate doctrine is to FERC's efforts at allocating the inevitable burdens stemming from fundamental readjustment of the pipeline industry.

On June 27, 1990, the court stayed issuance of its mandate pending the filing of a petition for a writ of certiorari by August 27, 1990. App. 29a.

REASONS FOR GRANTING THE PETITION

By finding "filed rate doctrine" impediments to the direct billing of unrecovered gas costs upon termination of a pipeline's sales service obligations (and the PGA clause), the court of appeals has ignored long-standing principles of statutory construction, defied well-established precepts concerning cost responsibility and cost incurrence, usurped FERC's broad statutory and discretionary authority to approve rates (or rate mechanisms) within the flexible parameters of the "just and reasonable" standard of Sections 4 and 5 of the NGA, 15 U.S.C. §§ 717c, 717d, and gone well beyond this court's prior interpretations of the "filed rate doctrine." The decision below, inasmuch as it leaves unresolved—and potentially unresolvable—cost recovery issues (with substantial industry-wide ramifications) presents pervasive and fundamental questions not heretofore considered by this Court.

Furthermore, the court of appeals' decision cannot be squared with decisions from other circuits which have considered, and accorded appropriate deference to, the scope of FERC's authority to craft "just and reasonable" rates without breaching "filed rate doctrine" principles. Indeed, the decision below is at odds with prior decisions of the same circuit and establishes new standards (and restrictions) for notice and waiver within the context of NGA rate regulation.

I. THE COURT BELOW HAS IGNORED FUNDAMENTAL PRINCIPLES OF STATUTORY CONSTRUCTION.

A. The Statutory Framework

Under Section 4(a) of the NGA, rates charged by an interstate pipeline for the sale or transportation of natural gas are deemed lawful to the extent they are "just and reasonable" within the meaning of the Act. Rate determinations under the "just and reasonable" standard are the exclusive province of the FERC; and, it is the end result—not the particular methodology employed—which must pass muster under the "just and reasonable" standard. *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 602 (1944) (*"Hope"*). Describing the "presumption of validity" which attaches to FERC's "expert judgement" and the deference owing to the Commission on review of rate determinations, the *Hope* court stated: "[i]f the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry under the Act is at an end." *Id.*

Under Section 4(d) of the NGA, rate changes proposed by an interstate pipeline are subject to a 30-day notice requirement which, absent a waiver for good cause shown, prohibits an interstate pipeline from collecting a rate other than the rate on file with the Commission. As this Court held in *Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571, 577 (1981) (*"Hall"*), this "filed rate doctrine" operates to preserve the agency's primary jurisdiction over the rates charged by regulated entities and ensures that these entities charge "only those rates of which the agency has been made cognizant." *Hall*, 453 U.S. at 578.

B. Application of Statutory Construction Principles

This court has consistently found that special deference is due the agency in matters involving the interpretation of statutory provisions within the agency's charge. *Chevron U.S.A. Inc. v. NRDC, Inc.*, 467 U.S. 837 (1984)

("*Chevron*").[28] As held in *Chevron*, a reviewing court considering a challenge to an agency's statutory construction is not free to substitute its judgement for that of the agency; rather, the construction rendered by the agency must be given effect so long as it represents a "reasonable choice within a gap left open by Congress." *Id.* at 866. Thus, courts must exercise a heightened degree of judicial restraint where the challenged agency action involves statutory construction pertinent to the exercise of authority left to the primary and "expert" judgement of the agency.

In the case below, the court rejected FERC's determination that the NGA Section 4(d) "notice" requirement: (i) was satisfied by any one of several, pre-1987 events or (ii) in any event could be waived, *in toto*, upon "good cause" shown. In so ruling, the court acted contrary to the teachings of *Hope* and *Chevron* by substituting its own statutory construction for that of FERC, and without giving even passing consideration to the "just and reasonable" end result achieved by the Commission's order. By eschewing the deference due FERC's statutory interpretation, and substituting its own interpretation of the "filed rate doctrine", the lower court also ignored this Court decision in *Hall*, and severely disrupted the agency's ongoing attempt to "reconcile conflicting policies" associated with the fundamental restructuring of the pipeline industry.

1. *FERC's Determination as to Adequacy of Notice*

The FERC reasonably determined that "notice" within the meaning of Section 4(d) had been furnished to Transwestern's customers no later than 1986 and as early as 1972 (with the promulgation of PGA regulations). These findings by FERC—reflecting nothing more or less than the agency's construction of its statu-

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[28] *See also K Mart Corp. v. Cartier, Inc.*, 486 U.S. 281 (1988) where the court held that if agency findings are not in conflict with the statute, "a reviewing court must give deference to the agency's interpretation." *Id.* at 292.

tory charge—are entitled to considerable weight and deference and, under *Chevron*, need only be "permissible" to withstand judicial review.

The court below transgressed from its limited judicial review responsibilities. Pursuing an inflexible and unnecessary factual analysis focusing on the "adequacy" of the notice (in terms of the rate methodology ultimately employed), and not the broader "end result" of the rate order, the court supplanted its judgement for that of FERC in precisely the manner proscribed by *Chevron*.

According to the court below, FERC's reliance on the 1972 PGA regulations (where the FERC explicitly assured pipelines' recovery of all purchased gas costs), as well as Transwestern's NGA Section 4 filings made in compliance with these PGA regulations (and which identified all under-recoveries or over-recoveries booked into Account No. 191), failed as notice to Transwestern's customers that deferred PGA balances would "follow them if the PGA system ended altogether." 897 F.2d at 580, App. 20a. Likewise, in the court's view, two 1986 decisions of the Commission—cited by FERC as alternative, albeit later, "notices" of the direct bill surcharge formula—could not constitute Section 4(d) notice that all PGA Account No. 191 balances would be charged to the customers on whose behalf they were incurred upon termination of the PGA.[29] And, while acknowledging that the deferred balances subject to the direct bill would have otherwise been recovered "under the [pre] existing PGA regulations, before the new Transwestern filing, under the same circumstances," 897 F.2d at 579, App. 18a, the court nonetheless determined that the PGA regulations themselves did not adequately alert Transwestern's customers of their cost responsibilities for all unrecovered PGA amounts to the extent such amounts were later assessed by way of direct bills.

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[29] The court also rejected Transwestern's position that its December 1, 1987 filing—which included the direct billing proposal—adequately alerted customers of their liability for direct bill payments of all unrecovered gas costs.

The court of appeals' rejection of FERC's "notice" determinations cannot be reconciled with *Chevron*'s statutory construction rules and the "end result" analysis mandated by *Hope*. First, the court never expressly found that the Commission's "notice" findings were "unreasonable" or "arbitrary, capricious or manifestly contrary to the statute." *Chevron*, 467 U.S. at 844. Rather, the court, at most, found such determinations lacking when analyzed in terms of the court's *own hypothetical* examples. But, judicial review parameters are considerably more circumscribed:

> The court need not conclude that the agency construction was the only one it permissibly could have adopted to uphold the construction, *or even the reading the court would have reached if the question initially had arisen in a judicial proceeding* . . . . [C]onsiderable weight should be accorded to an executive department's construction of a statutory scheme it is entrusted to administer, *and the principle of deference to administrative interpretations 'has been consistently followed whenever decision as to the meaning or reach of a statute has involved reconciling conflicting policies . . . .'*

Id., at 843-44 (citations omitted, emphasis added).

Ironically, the lower court's earlier decision in *Public Service* supports FERC's notice findings, and the court's attempt to distinguish *Public Service* fails as grounds for rejecting FERC's notice findings in the instant case. Just as in *Public Service*, the issue presented below concerned the "utility's ability to collect for costs that were left over as a result of transition from one billing system to another." 897 F.2d at 578, App. 15a. Yet, in *Public Service*, the court reasoned that where customers are fully apprised of their responsibility for the subject costs, more definitive notice of the specific rate is not required. Stated differently, *Public Service* is fairly read to stand for the proposition that the timing of the customer's awareness of the exact rate or *precise methodology* to be employed for recovery of costs is not the deciding event for determining notice under the filed rate doctrine.

Citing *Public Service*, the court below conceded that an approved rate formula could serve as the basis for prior period rate adjustments. Yet, the court failed to embrace the 1972 PGA regulations and the operation of Transwestern's PGA tariff provisions—and the cost recovery rights established thereunder—as acceptable notice under Section 4 of the NGA entitling Transwestern to full recovery of deferred PGA balances following implementation of its GIC. In the court's view, because the cost recovery *mechanism—i.e.*, the direct bill—changed (arguably) without "adequate" notice, Transwestern should be denied recovery of purchased gas costs which were (i) incurred on behalf of Transwestern's sales customers at a time when such customers had contractual and service rights to purchase gas from Transwestern; and (ii) otherwise recoverable through the PGA tracking mechanism in place at the time Transwestern incurred the costs, as well as the PGA surcharge mechanism which also was in place at the time the costs were incurred and remained in effect until the effectiveness of the GIC mechanism.

FERC's reliance on the 1972 PGA regulations (or, alternatively, the two 1986 orders approving comparable direct bill mechanisms) as Section 4(d) "notice" to Transwestern's customers of their cost responsibility for unrecovered, outstanding PGA balances, was clearly within the "permissible" and/or "reasonable" zone and was therefore entitled to effect. Moreover, the "end result" produced by the court's interpretation—*i.e.*, outright denial of Transwestern's ability to recover certain purchased gas costs—contravenes the express provisions of NGPA Section 601(c) and cannot, therefore, be sustained as "reasonable." *See* discussion *infra*. Thus, this is not an instance where the court displaced an agency's unreasonable interpretation with a reasonable one, or even where a permissible interpretation was replaced in favor of one deemed "preferable" or "more reasonable"; rather, FERC's proper and lawful interpretation was denied effect in lieu of the court's impermissible inter-

pretation.[30] A more compelling case for judicial restraint and deference to the agency can hardly be imagined; the court below overstepped its authority by rejecting FERC's reasonable and equitable solution to the residual cost responsibility issues left in the wake of the "open-access" transition.[31]

2. *Waiver of Notice*

In addition, the court of appeals decision effectively reads out of Section 4(d) of the NGA the express authority vested in FERC to waive the notice requirement.

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[30] By substituting its own construction of notice—and drawing the line at May 11, 1988—the court compounded its initial error. That is, to the extent that the court below could not sustain FERC's notice finding, the proper response would have been a remand to the agency for further determinations, consistent with court-prescribed guidelines. *See City of Willcox v. FPC*, 567 F.2d 394, 409-410 (D.C. Cir. 1977), *cert. denied*, 434 U.S. 1012 (1978), (directing that issue of cutoff date for users seeking broader entitlements under FERC-approved curtailment plan be decided on remand to the Commission.)

[31] Moreover, in direct conflict with the underlying principle of the doctrine, the court's finding of "filed-rate" obstacles to recovery of gas costs serves to undermine (rather than preserve) FERC's primary jurisdiction over pipeline rates and terms of service. The court's decision—and the refusal to accord liberal deference to the agency's statutory construction—flies in the face of a formidable line of precedent noting the primary, if not exclusive, jurisdiction of FERC to regulate rates under Sections 4 and 5 and to enforce terms of service under Section 7. *See e.g., Hall*, 453 U.S. at 577 (noting FERC's exclusive rate jurisdiction); *see also Shell Oil Co. v. FERC*, 566 F.2d 536 (5th Cir. 1978), *aff'd*, 440 U.S. 192 (1979) (noting FERC's exclusive jurisdiction over terms of certificated service). This, of course, is not to suggest that FERC rate or certificate determinations are not judicially reviewable; rather, principles of judicial restraint and deference are simply of greater moment when challenges are brought regarding such determinations. *See Water Transport Ass'n v. ICC*, 715 F.2d 581, 592, n.26 (D.C. Cir. 1983), *cert. denied*, 465 U.S. 1006 (1984). The anomalous result produced by the lower court's decision shackles FERC to the point of leaving it hamstrung in its ability to regulate the industry. Such result surely could not have been intended by the NGA drafters in enacting the broad and "pervasive regulatory scheme" entrusted to FERC.

The court's interpretation of the "filed rate doctrine", and the nominal proscriptions against retroactive rate changes, ignores the statute's explicit proviso that, for good cause, the Section 4(d) notice requirement may be waived.

Consistent with the unambiguous terms of the statute, and even assuming *arguendo* that direct billing of gas costs somehow constitutes retroactive ratemaking, the exclusive prerequisite for waiver of the filed rate notice requirement—*i.e.* "good cause"—was, as FERC found, satisfied. 44 F.E.R.C. at 61,537, App. 113a. Considerations no less critical than the preservation of the cost incurrence/cost causation principle led FERC to the "end result" of approving Transwestern's direct billing proposal.

According to the lower court, its recent *Columbia II* decision disposes of FERC's waiver argument because notice to the rate-payers in advance of the actual rate-change filing with FERC "changes what would be purely retroactive ratemaking into a functionally prospective process." 895 F.2d at 797. But, as FERC has argued in its petition to this Court seeking a writ of certiorari in *Columbia II*, the court's creation of an extra-statutory and non-waivable notice requirement finds no support in the plain language of Section 4(d) and does not—contrary to the court's finding—neutralize the retrospective nature of the changed rate. As FERC correctly observed

> the increase would have been retrospective in at least one respect that seems especially relevant for purposes of the filed rate doctrine, because it still would have applied to sales made prior to the date the rate change was filed with the Commission.

Petition for a Writ of Certiorari at 18, *FERC v. Columbia Gas Transmission Corp.*, Case No. 90-131. The Commission's construction of its statutory "waiver" authority—*i.e.* permitting, for good cause, rate changes without

advance notice to the rate-payers and before filing with the Commission—is certainly as reasonable as the *Columbia II* construction and, in any event, does not "do violence" to the statute.

Moreover, and notwithstanding its attempts at reconciliation, the court's holding in *Columbia II* concerning waiver (as relied upon in the case below to deny Transwestern rate coverage for certain purchased gas costs) cannot be squared with its earlier decision in *City of Piqua v. FERC*, 610 F.2d 950 (D.C. Cir. 1979) ("*Piqua*"). *Columbia II* characterizes *Piqua* as essentially a "notice" case—*i.e.* where the agreement between the parties served as "notice" authorizing a yet, unfiled rate change. But, the language of the *Piqua* decision unambiguously establishes it as a "waiver" case, noteworthy for its pronouncements concerning the FERC's authority to dispense with the statutory notice requirement for good cause shown. Rejecting "filed rate doctrine" and retroactive ratemaking challenges to a FERC order authorizing a pre-filing effective date for a change in rates, the *Piqua* court stated:

> '*The considerations underlying the* [*filed rate*] *doctrine . . . . are preservation of the agency's primary jurisdiction over reasonableness of rates* and the need to insure that regulated companies charge only those rates of which the agency has been made cognizant.' *This purpose is unaffected by the Commission's waiver of the notice requirement upon good cause*, thus allowing rate changes, found by the Commission to be just and reasonable, to become effective on the date agreed by the parties.
>
> We have considered the agency's interpretation of section 205(d) in light of the Act's policy and the practical consequences of the proposed construction. *We find that section 205(d) statutorily authorizes the Commission's waiver of the prior notice requirement upon a showing of good cause.*

Id. at 955 (emphasis added, citations omitted).

Even assuming, *arguendo*, that *Columbia II* and *Piqua* (as applied in the case below) stand for the proposition that notice to customers is a non-waivable prerequisite to the retrospective collection of rates later filed with FERC, such notice as discussed *supra* existed here. The Commission's regulations regarding recovery of purchased gas costs, and the operation of Transwestern's related PGA tariff provisions, provided notice to Transwestern's customers that they remained responsible for all gas costs prudently incurred on their behalf—a responsibility which would remain "for costs that were left over as a result of transition from one billing system to another." *Transwestern*, 897 F.2d at 578, App. 15a, citing *Public Service*, 600 F.2d at 948. Thus, even under the lower court's *Columbia II* rationale, there existed the requisite notice that Transwestern was authorized to collect all PGA balances remaining in Account No. 191 upon termination of Transwestern's PGA. To reject outright both the notice findings by FERC, as well as the waiver authority asserted by FERC, is to deny effect to the agency's reasonable interpretation of the operative statute—a statute which, by its terms, vests in FERC the exclusive jurisdiction to regulate pipeline sales and transport rates. Having failed to establish that FERC's notice findings and statutory construction of the "waiver" provision was "impermissible", or "unreasonable", or "arbitrary or capricious," the court's rejection of such findings and construction cannot stand. *See Chevron*, 467 U.S. at 843-44, *see also Piqua*, 610 F.2d 950 [32]; *Hall v. FERC*,

[32] As noted, in *Piqua*, the court found good cause—*i.e.* an agreement between the parties—for waiver of the notice requirement to permit a changed rate to become effective before the filing of such change with the Commission. 610 F.2d at 954-55. Here, the costs at issue were incurred for the benefit of Transwestern's sales customers who had *both* contractual and service obligations to pay for supplies taken. Thus, the signed service agreements between Transwestern and its sales customers, together with the unassailable notion—established by the PGA regulations and Section 601 of the NGPA—that gas costs would be fully recoverable absent fraud or abuse, established good cause for waiver of any arguably unsatisfied notice requirement.

691 F.2d 1184 (5th Cir. 1982), *cert. denied*, 464 U.S. 822 (1983); *Towns of Concord and Wellesley v. FERC*, 844 F.2d 891, 896-897 (1st Cir. 1988).

II. CONFLICT WITH NGPA AND PGA REGULATIONS

Section 601(b) of the NGPA, 15 U.S.C. § 3431(b), provides that for purposes of Sections 4 and 5 of the NGA, any amount paid in any first sale of natural gas shall be deemed to be just and reasonable if such amount does not exceed the applicable maximum lawful price established under Title I of the NGPA or, if there is no applicable maximum lawful price, solely by reason of the elimination of price controls pursuant to the deregulation provisions of Title I of the NGPA. In addition, Section 601(c), entitled "Guaranteed passthrough" states

> For purposes of sections 4 and 5 of the Natural Gas Act, *the Commission may not deny any interstate pipeline recovery of any amount paid with respect to any purchase of natural gas* if, under subsection (b) of this section, such amount is deemed to be just and reasonable for purposes of sections 4 and 5 of such Act, *except to the extent the Commission determines that the amount paid was excessive due to fraud, abuse, or similar grounds.*

15 U.S.C. § 3431(c) (emphasis added).

Thus, Transwestern has a statutory entitlement to recovery of gas costs—whether as undercollections recorded in Account No. 191 or otherwise—if it demonstrates that such costs are (i) costs paid for the purchase of natural gas and, (ii) do not exceed the NGPA Title I price ceilings and (iii) are not excessive due to fraud, abuse, imprudence or other grounds.

Significantly, the court below did not propose a different "end result" which would satisfy the guaranteed passthrough mandate of Section 601(c), and at the same time ameliorate the court's concerns regarding notice and/or waiver. In addition (and as has been discussed *supra*), the lower court's decision stands in fundamental contrast to the principles and purposes of FERC's PGA

regulations which have governed gas cost recovery since 1972. These regulations unequivocally provide for timely and full recapture of all amounts paid by pipeline suppliers in connection with gas acquisitions for jurisdictional sales. To digress on an irrelevant and tedious notice analysis—*i.e.* which focused not on the question of whether customers had reasonable notice of their *responsibility* for costs incurred on their behalf (which they most certainly did), but rather on whether a *precise recovery mechanism* had to be made known to them in advance of the accrual of costs—is to exalt form over substance in a manner that ignores not only the fundamental precepts of cost causation and pipeline ratemaking, but also the statutory requirements of Title VI of the NGPA.

III. THE D.C. CIRCUIT'S OPINION CONFLICTS WITH DECISIONS RENDERED BY OTHER FEDERAL COURTS OF APPEALS.

The Fifth and Tenth Circuits have also rendered decisions on FERC's attempts to deal with cost recovery issues in light of the revolution occurring within the natural gas industry as a result of both Congressional and FERC initiatives. *See, Texas Eastern Transmission Corp. v. FERC*, 769 F.2d 1053 (5th Cir. 1985), *cert. denied sub nom. Associated Gas Distributors v. FERC*, 476 U.S. 1114 (1986) (*"Texas Eastern"*), and *Phillips Petroleum Co. v. FERC*, 902 F.2d 795 (10th Cir. 1990) (*"Phillips"*). Specifically, both circuits have rejected challenges to FERC orders providing for retroactive recovery of production-related costs pursuant to Section 110 of the NGPA, 15 U.S.C. § 3320. These circuits, with proper deference to FERC's interpretation of statutory provisions within its charge, upheld the challenged orders in the face of allegations that direct billing of past period production-related costs contravened the filed rate doctrine and the proscription against retroactive ratemaking.

In *Texas Eastern*, the Fifth Circuit reviewed FERC Order Nos. 94 and 94-A,[33] which established allowances applicable to, and/or procedures for collection of, production-related costs pursuant to NGPA Section 110. More specifically, Order No. 94 authorized immediate collection of certain production-related costs, *e.g.* for dehydration, but deferred to a later date the establishment of procedures for recovery of compression and delivery allowances which, once implemented, would provide for retroactive recovery of all qualifying costs incurred after the effective date of Order No. 94.

In upholding the FERC orders, the *Texas Eastern* court properly deferred to FERC's "balancing of the various problems involved . . .," 769 F.2d at 1066, to sustain the "end result" fashioned by FERC. Agreeing with FERC's "notice" determinations, the court in *Texas Eastern* found no "filed-rate doctrine" obstacles to the retroactive recovery of qualifying production-related costs so long as the affected customers were apprised, generally, of their cost responsibilities. That the precise procedure for the recovery of such costs was not established until a later date did not undermine FERC's "notice" findings or bar the retroactive recovery of the Order No. 94 allowances.

Similarly, in *Phillips*, the Tenth Circuit reviewed Order Nos. 473 and 473-A [34] which were issued in response to the Fifth Circuit's *Texas Eastern* mandate. The FERC orders under review in *Phillips* implemented (1) procedures for protesting production-related cost allowances

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[33] *Order Amending Interim Regulations Under the Natural Gas Policy Act of 1978 and Establishing Policy Under the Natural Gas Act*, Order No. 94, FERC Stats. & Regs. [Regulations Preambles 1977-81] ¶ 30,178 (1980), *reh'g granted in part and denied in part*, Order No. 94-A, FERC Stats. & Regs. [Regulations Preambles 1982-85] ¶ 30,419 (1983).

[34] *Compression Allowances and Protest Procedures Under NGPA Section 110*, Order No. 473, FERC Stats. & Regs. [Regulations Preambles] ¶ 30,747, *modified*, Order No. 473-A, FERC Stats. & Regs. [Regulations Preambles] ¶ 30,788 (1987).

for all categories of NGPA gas, whether or not the gas was subject to FERC's NGA jurisdiction, and (2) fuel and power allowances for pre-NGPA systems and provided that interest on retroactive collections of such allowances for the period between issuance of Order No. 94-A and Order No. 473 required express contractual authority. The Tenth Circuit reaffirmed that Order No. 94, issued in 1980, provided "proper notice" to allow (in 1983, with the issuance of Order No. 94-A) retroactive collection of production-related costs.[35]

In contrast to the Fifth and Tenth Circuit decisions, the lower court has adopted a narrow view of FERC's ratemaking powers and invoked its own rigid statutory interpretation of the "filed rate doctrine" and the prohibition against retroactive ratemaking in striking down FERC orders attempting to achieve a just and reasonable resolution with respect to purchased gas costs which remain unrecovered at the termination of the sales service agreements and the PGA clause. The findings of the court below with regard to the "filed-rate doctrine" and, in particular, the "notice" required to defeat a "filed-rate doctrine" challenge, conflict with holdings in both the Fifth and Tenth Circuits.[36] A review of the *Texas East-*

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[35] The court of appeals also deferred to FERC's finding that, because retroactive collection of the allowances was permitted, it would only be equitable to allow protests to collection of those allowances. In addition, the Tenth Circuit found sufficient notice for requiring express contractual authority for collection of interest on fuel and power allowances for pre-NGPA systems in Order No. 94-A, which required express contractual authority to collect interest on fuel and power allowances for post-NGPA systems.

[36] It bears noting that the instant case is the third in a series of cases recently decided by the D.C. Circuit, *see also, AGD II* and *Columbia II*, dealing with the NGA Section 4(d) notice requirement. All such cases arise in the context of FERC's attempts to set "just and reasonable" rates following the "recent dramatic changes in the structure of the natural gas industry." *Transwestern Pipeline Co. v. FERC*, Case Nos. 88-1046, *et al.*, separate statement of Chief

ern and *Phillips* decisions reveals a split of authority between the Fifth and Tenth Circuits (on the one hand) and the D.C. Circuit (on the other) with respect to principles of statutory construction and deference owing to administrative agencies. Inasmuch as different circuits have adopted different standards and reached different decisions regarding the Commission's authority to interpret and implement its organic statutes and fashion "just and reasonable" end results to the transitional issues arising in the post-Order Nos. 436/500 environment, Transwestern respectfully urges that the instant petition for certiorari be granted.

CONCLUSION

For the reasons stated herein, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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Judge Wald to Denial of Suggestions for rehearing *en banc*, May 31, 1990, App. 28a.

In addition to being inconsistent with the pronouncements of this Court, and holdings of the Fifth and Tenth Circuits, these three decisions, also conflict with previous decisions rendered by the D.C. Circuit, despite that court's attempts at reconciliation. *See, Piqua* and *Public Service, supra.*

APPENDIX

APPENDIX

UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

Argued October 30, 1989 Decided March 23, 1990

No. 88-1046

TRANSWESTERN PIPELINE COMPANY,
Petitioner

v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent

THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA,
PROCESS GAS CONSUMERS GROUP,
SOUTHERN CALIFORNIA GAS COMPANY,
EL PASO NATURAL GAS COMPANY,
PACIFIC GAS AND ELECTRIC COMPANY,
TEXAS EASTERN TRANSMISSION CORPORATION,
THE KANSAS POWER AND LIGHT COMPANY,
SOUTHWEST NATURAL GAS CORPORATION,
WILLIAMS NATURAL GAS COMPANY,
Intervenors

No. 88-1371

TRANSWESTERN PIPELINE COMPANY,
Petitioner

v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent

SOUTHERN CALIFORNIA GAS COMPANY,
SOUTHWEST GAS CORPORATION,
PACIFIC GAS AND ELECTRIC COMPANY,

WILLIAMS NATURAL GAS COMPANY,
PUBLIC UTILITIES COMMISSION OF THE
STATE OF CALIFORNIA,
EL PASO NATURAL GAS COMPANY,
CITIZENS ENERGY CORPORATION, *et al.*,
Intervenors

No. 88-1484

TRANSWESTERN PIPELINE COMPANY,
Petitioner

v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent

WILLIAMS NATURAL GAS COMPANY,
SOUTHERN CALIFORNIA GAS COMPANY,
PUBLIC UTILITIES COMMISSION OF THE
STATE OF CALIFORNIA,
Intervenors

No. 88-1555

TRANSWESTERN PIPELINE COMPANY,
Petitioner

v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent

KANSAS POWER & LIGHT COMPANY,
NATURAL GAS CLEARINGHOUSE, INC.,
WILLIAMS NATURAL GAS COMPANY,
SOUTHERN CALIFORNIA GAS COMPANY,
PUBLIC UTILITIES COMMISSION OF THE
STATE OF CALIFORNIA,
PACIFIC GAS & ELECTRIC COMPANY,
PSI, INC.,
TEXAS EASTERN TRANSMISSION CORP.,
SOUTHWEST GAS CORP.,
Intervenors

No. 88-1559

PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA,
Petitioner

v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent

KANSAS POWER & LIGHT COMPANY,
NATURAL GAS CLEARINGHOUSE, INC.,
WILLIAMS NATURAL GAS COMPANY,
SOUTHERN CALIFORNIA GAS COMPANY,
PACIFIC GAS & ELECTRIC COMPANY,
PSI, INC.,
SOUTHWEST GAS CORP.,
TRANSWESTERN PIPELINE COMPANY,
Intervenors

No. 88-1573

KANSAS POWER & LIGHT COMPANY,
Petitioner

v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent

NATURAL GAS CLEARINGHOUSE, INC.,
WILLIAMS NATURAL GAS COMPANY,
PACIFIC GAS & ELECTRIC COMPANY,
PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA,
SOUTHERN CALIFORNIA GAS COMPANY,
PSI, INC.,
TRANSWESTERN PIPELINE COMPANY,
Intervenors

Petitions for Review of an Order of the
Federal Energy Regulatory Commission

Harvey Y. Morris and *Martin J. Bregman*, with whom *Janice E. Kerr*, *J. Calvin Simpson*, for Public Utilities Commission of the State of California, *John K. Rosenberg*, *William I. Harkaway* and *Harvey L. Reiter*, for the Kansas Power and Light Company, were on the joint brief, for Public Utilities Commission of the State of California, et al., petitioners in Nos. 88-1559, 88-1573 and intervenors in Nos. 88-1046, 88-1371, 88-1484 and 88-1555.

William J. Grealis, with whom *Jeffrey G. DiSciullo*, *Frederick W. Peters*, *Dana B. Ott*, *Sherrie N. Rutherford*, *Cheryl M. Foley*, *Charles A. Moore*, *Marilyn L. Doria* and *Robert W. Gee*, were on the brief, for Transwestern Pipeline Company, petitioner in Nos. 88-1046, 88-1371, 88-1484, 88-1555, and intervenor in Nos. 88-1559 and 88-1573.

Dwight C. Alpern, Attorney, Federal Energy Regulatory Commission, with whom *Catherine C. Cook*, General Counsel, and *Jerome M. Feit*, Solicitor, Federal Energy Regulatory Commission, were on the brief, for respondent in all cases. *Hanford O'Hara*, Attorney, Federal Energy Regulatory Commission, also entered an appearance for respondent.

Douglas Kent Porter and *E.R. Island* entered appearances for intervenor Southern California Gas Company in Nos. 88-1046, 88-1371, 88-1484, 88-1555, 88-1559, and 88-1573.

Joshua Bar-Lev, *Steven F. Greenwald* and *Lindsey How-Downing* entered appearances for intervenor Pacific Gas and Electric Company in Nos. 88-1046, 88-1371, 88-1555, 88-1559 and 88-1573.

Gregory Grady and *Douglas O. Waikart* entered appearances for intervenor Williams Natural Gas Company in Nos. 88-1046, 88-1371, 88-1484, 88-1555, 88-1559 and 88-1573.

Edward J. Grenier, Jr., *William H. Penniman*, and *James M. Bushee* entered appearances for intervenor Process Gas Consumers Group in No. 88-1046.

William I. Harkaway, *Douglas M. Canter* and *Steven J. Kalish* also entered appearances for intervenor Southwest Gas Corporation in Nos. 88-1046, 88-1371, 88-1555 and 88-1559.

Judy M. Johnson and *John S. Carr* entered appearances for intervenor Texas Eastern Transmission Corp., in Nos. 88-1046 and 88-1555.

Richard C. Green, *Donald J. MacIver, Jr.*, *Richard Owen Baish* and *Michael D. Ferguson* entered appearances for intervenor El Paso Natural Gas Company in Nos. 88-1046 and 88-1371.

Peter G. Esposito entered an appearance for intervenor Natural Gas Clearinghouse, Inc., in Nos. 88-1555, 88-1559 and 88-1573.

Daniel C. Kaufman and *James U. Hamersley* entered appearances for intervenor PSI, Inc., in Nos. 88-1555 and 88-1559.

Before: WILLIAMS, D.H. GINSBURG and SENTELLE, *Circuit Judges.*

Opinion for the Court filed by *Circuit Judge* WILLIAMS.

WILLIAMS, *Circuit Judge*: This appeal grows out of the Federal Energy Regulatory Commission's attempt to afford natural gas consumers the benefits of increased competition. Its basic stratagem was to "unbundle" the sale of gas from its transportation, enabling local distribution companies and end-users to buy gas in the field and to use interstate pipelines simply for transportation.

See Order No. 436, *Regulation of Natural Gas Pipelines after Partial Wellhead Decontrol*, 50 Fed. Reg. 42,408 (1985). In *Associated Gas Distributors v. FERC*, 824 F.2d 981 (D.C. Cir. 1987), this court upheld the substance of the Commission's new approach, but vacated and remanded Order No. 436 because the Commission had failed to address adequately the effect of its new regulations on the interstate pipelines' take-or-pay liability. Because Order No. 436 put pressure on pipelines to allow shipments of gas in competition with their own supplies, it increased their difficulties in selling (without loss) quantities of gas that they were obligated to either take or pay for. On remand, the Commission sought to offset these difficulties by shifting some of the costs onto producers and customers. See Order No. 500, *Regulation of Natural Gas Pipelines after Partial Wellhead Decontrol*, 52 Fed. Reg. 30,334 (1987). Challenges to the order were consolidated into one complex case, the first phase of which addressed a facial challenge to the entire order, and the second phase of which considered the application of the Commission's "equitable sharing" policy to a particular pipeline. See *American Gas Association v. FERC*, 888 F.2d 136 (D.C. Cir. 1989) (Phase I); *Associated Gas Distributors v. FERC*, 893 F.2d 349 (D.C. Cir. 1989) (Phase II).

This segment of the case was intended to address issues raised by a so-called gas inventory charge, also known by the acronym GIC. Here the Commission's object was to define the limits on pipelines' ability to charge their customers for the costs of maintaining an inventory of contract rights to purchase gas (including one form those costs may take, namely liability under contracts requiring a pipeline to take gas or pay for it anyway), and thereby to prevent recurrence of the recent take-or-pay pass-through issues.[1] The Commission originally discussed

[1] We deferred addressing the validity of the GIC policy statement in Phase I of these complex proceedings because it was unripe until applied in a concrete setting. See *AGA*, 888 F.2d at 152.

the charge as a policy statement within Order No. 500 and later implemented it in a number of specific decisions, including the one now before us.

Although a large number of cases were filed challenging FERC implementation of the gas inventory charge, the present case was jointly selected by the parties as the most suitable one for its review; the remainder were held in abeyance. As will be developed below, most of the key issues in this case have been rendered moot. The only customers of Transwestern potentially affected by Transwestern's gas inventory charge proposals have ceased to purchase gas from that pipeline, and nothing before us suggests that any judicial correction of FERC's asserted errors would restore gas sales transactions. A number of peripheral issues survive mootness, but the upshot is that this case has failed as the selected vehicle for review of the Commission's actions on gas inventory charges.

I

Before turning to the Commission's disposition of Transwestern's gas inventory charge proposal, we must first clear out of the way Transwestern's attack on the Commission's rejection of its earlier filing, in June 1986, of a proposal for a somewhat similar charge, then called a "supply reservation charge." [2] The Commission rejected the filing and set it down for a hearing. 36 FERC ¶ 61,048 at 61,104 (1986). After hearing, the ALJ rejected the proposal, 39 FERC ¶ 63,025 (1987), and the Commission affirmed. 40 FERC ¶ 61,324 at 61,994-95 (1987). The Commission found the proposed charge too vague since crucial terms—such as the amount of the charge and its relation to Transwestern's actual cost of reserving supplies—depended on the outcome of negotia-

[2] It also sought to recover from its firm sales customers 100% of its costs in buying out and buying down existing take-or-pay contracts. The Commission rejected this part of the filing and Transwestern has not sought review of that rejection here.

tions with Transwestern's producers, which it had not then completed. *Transwestern*, 40 FERC at 61,995.

Transwestern tells us that the Commission's objection, the proposal's lack of specific figures, is of no weight: Transwestern offered the supply reservation charge only as a "mechanism." We do not believe that as an ordinary matter a pipeline's attachment of the "mechanism" label requires the Commission to dispense with insistence on specific figures. Of course that may be so where a pipeline offers to establish that market forces will hold charges to just and reasonable levels and submits adequate support for the claim. But in the absence of some such special circumstance the Commission's position seems entirely reasonable. Here, although the proposed charge was designed to cover Transwestern's cost of maintaining gas supplies, Transwestern could offer no actual evidence of the costs because it had not yet completed negotiations with any of its producers. *Id.* The Commission was surely not arbitrary or capricious in declining "to allocate risks and unknown future costs between the pipeline and its customers in a vacuum." 40 FERC at 61,996.

Transwestern also complains that FERC applied its Order No. 500 policy statement after the record was closed and even though its proposal was filed before Order No. 500. This is simply not true. After rejecting Transwestern's proposal as "not sufficiently developed," the Commission noted that any new proposal should look to the principles stated in Order No. 500. 40 FERC at 61,995. Where an agency has rejected a proposal on legitimate standards, its offer of a helpful hint as to criteria for the future is not the same as reliance on the latter.

II

After Transwestern's 1986 filing was rebuffed, it submitted in December 1987 a filing under § 4 of the Natural Gas Act, 15 U.S.C. § 717c (1988), in which it sought

to avoid future take-or-pay problems by implementing a gas inventory charge in accordance with Order No. 500. Under the proposal, a customer would nominate in advance the amount of gas it intended to buy from Transwestern for a specified period. Before nominations were due, Transwestern would publish the relevant prices —rate schedules for the purchase of gas, and the gas inventory charge, i.e., a charge for each unit of gas nominated but *not* taken, somewhat equivalent to a liquidated damages clause in a longterm purchase contract. Joint Appendix ("J.A.") 225-26, 242, 256-58. The actual amount of the charges would be up to Transwestern, which argued that competitive market forces would keep them at just and reasonable levels. *Id.* at 263-64.

In a companion filing under § 7 of the Natural Gas Act, 15 U.S.C. § 717f, Transwestern proposed that whenever a customer's nomination fell below its certificated firm sales entitlement, the unused entitlement would be automatically abandoned and converted to an entitlement to firm transportation. J.A. 228-29.

The Commission rejected the § 4 filing because it found that the service to be provided was not covered by Transwestern's existing certificate, and redocketed the whole matter for hearing and decision under § 7. See *Transwestern Pipeline Co.*, 41 FERC ¶ 61,371 (1987) (Order Redocketing Filing); 42 FERC ¶ 61,370 (1988) (Order Denying Rehearing). The Commission later accepted the proposal, subject to two conditions, of which more will be said later. 43 FERC ¶ 61,240 (1988) (Order); 44 FERC ¶ 61,164 (1988) (Order Granting Rehearing in Part and Clarifying Prior Order).

Attacks on the Commission's action come from two sides. Transwestern itself attacks the decision to redocket the entire proposal under § 7, which prevented its new rates from going into effect promptly under § 4. It also attacks the two conditions attached by the Commission. On the other side, two parties that we will loosely call

downstream purchasers attack the Commission's conclusion that market forces will hold Transwestern's rates to just and reasonable levels, and attack the gas inventory charge as equivalent to "minimum bills," which the Commission has previously found (for most contexts) inconsistent with just and reasonable rates. See, e.g., Order No. 380, *Elimination of Variable Costs from Certain Natural Gas Pipeline Minimum Commodity Bill Provisions*, Stats. & Regs. [Regulations Preambles] ¶ 30,571 (1984) at 30,970-71 (eliminating recovery in minimum bills of take-or-pay costs), aff'd, *Wisconsin Gas Co. v. FERC*, 770 F.2d 1144 (D.C. Cir. 1985); see also *Transwestern Pipeline Co.*, 32 FERC ¶ 61,009 at 61,031 (1985) (eliminating fixed-cost minimum bill entirely in order to prohibit guaranteed recovery of equity return, related taxes, and fixed production costs), aff'd, *Transwestern Pipeline Co. v. FERC*, 820 F.2d 733 (5th Cir. 1987). They also attack the Commission's decision to allow Transwestern to bill its customers for the accumulated balance in its so-called Account No. 191, an account used to implement the "purchased gas adjustment" or "PGA" that pipelines have been allowed but that would terminate under Transwestern's proposal.

One of the two parties asserting these latter views, Kansas Power & Light Company, is in fact a downstream purchaser, buying supplies from Transwestern's customer Williams Natural Gas Company; the other, the California Public Utilities Commission, is a state regulatory agency seeking to advance the interests of downstream purchasers from another Transwestern customer, Southern California Gas Company ("SoCal").

Transwestern has only two customers who are potentially affected by the forward-looking aspects of the Commission's decision, Williams and SoCal. Both have elected to purchase no gas from Transwestern under the new scheme. As we shall develop below, this moots most of the attacks made by both sides. It leaves in place, how-

ever, the downstream purchasers' contention that Transwestern's scheme for disposition of its Account No. 191 balance violates the rule against retroactive ratemaking, and an aspect of Transwestern's attack on the conditions attached by the Commission.

Mootness of Attack on GIC Mechanism

A case is moot if events have so transpired that the decision will neither presently affect the parties' rights nor have a more-than-speculative chance of affecting them in the future. See, e.g., *Friends of Keeseville, Inc. v. FERC*, 859 F.2d 230, 234 (D.C. Cir. 1988) (review may not be premised on "bare possibility" that agency action would lead to injury); Wright, Miller, Cooper, *Federal Practice and Procedure* § 3533.3 at 273-74 (1984) (moot if prospect of future effects "too remote to justify decision").

Here, both Williams and SoCal—Transwestern's only customers possibly affected by the GIC under review here—have elected not to purchase any gas from Transwestern under the newly approved certificate. Williams exercised its option to terminate its sales service agreement with Transwestern on February 1, 1988, to take effect February 1, 1989. See J.A. 380-81. SoCal continued its relationship longer, but on September 15, 1989 elected under the provisions of the Transwestern tariff approved here to nominate purchases of zero, thereby converting its entire sales entitlement to transportation. See Motion of Transwestern Pipeline Company to Lodge Documents and Suggestion of Possible Mootness, Appendix A. As a result, regardless of a decision by this court on the merits of the challenged gas inventory charge, the downstream purchasers acknowledge that "no GIC charges will ever be assessed against [Transwestern's] customers." Answer of the Kansas Power and Light Company and the Public Utilities Commission of the State of California to Motion of Transwestern Pipeline

Line [sic] Company to Lodge Documents and Suggestion of Possible Mootness ("Answer") at 2. Accordingly these petitioners cannot be affected by the gas inventory charge or by whatever ruling we might make on it.[3]

The downstream purchasers suggest that future effects are likely by arguing that Commission approval of Transwestern's proposals "coerce[d]" SOCal into permanently abandoning its sales service. *Id.* at 3. (No one makes this suggestion as to Williams, which terminated its sales service from Transwestern after the latter filed its proposals but on the basis of prior arrangements and before the Commission approved Transwestern's proposal.) Assuming that a favorable decision on the downstream purchasers' claims would entitle SoCal to reverse that election, such a decision could favorably affect them. But the benefit for the downstream purchasers could arise only if SoCal were actually to seek to reverse its earlier decision. Far from doing so, it displays a complete lack of interest in this appeal even though it was actively engaged in the proceedings below. Indeed, even before Transwestern's filing of its gas inventory charge proposals, SoCal had been steadily shifting its relation with Transwestern from gas purchaser to transportation user, buying its gas elsewhere. See Transwestern's October 1987 Request for Rehearing of the Commission's denial of its 1986 filing, J.A. 156. Without so much as a nod

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[3] This is not a case where the parties have challenged the validity of both an ongoing practice and a now moot application of that practice. In such a case, this court has held the specific application moot, but gone on to decide the more general claim. See, e.g., *Payne Enterprises, Inc. v. U.S.*, 837 F.2d 486, 490-91 (D.C. Cir. 1988) (suit to compel disclosure of documents made under FOIA request moot as to documents subsequently disclosed, but not as to challenge to agency "policy or practice" which resulted in initial denial of request). Here, by contrast, no party challenges the general validity of the policy statement regarding gas inventory charges in Order No. 500, and in any event we have already held the policy statement by itself unripe for review. *AGA*, 888 F.2d at 152.

from SoCal (or some authoritative statement reconciling the absence of a nod with the purchasers' image of SoCal as victim), the causal chain is far too tenuous.

Finally, the downstream purchasers argue that because Transwestern's billing of the balance of its Account No. 191 is not moot (on which we agree), we must decide the validity of the gas inventory charge because it was "the predicate" of the Commission's approval of the Account No. 191 billing. Answer at 7. While it is true that Transwestern's attempted shift to sales under a gas inventory charge precipitated its proposal for billing of Account No. 191 balances, *any* end of its purchased gas adjustment system would have raised the same issue. The link to the gas inventory charge is quite fortuitous. There is no reason why the Account No. 191 tail should wag the gas inventory charge dog back to life.

Billing of Prior Gas Cost Balances ("Account No. 191") to Departing Customers

Transwestern's 1987 filing entailed a complete alteration of its rates for "bundled" service, i.e., its own sales of gas at the end of its pipeline. Formerly the gas component was based on forward projections of historical costs, with provision for adjustment in the next period for any differences; thereafter, competition was expected to hold the gas component to the level of true economic costs. This created a transition problem—the treatment of the leftover differences between Transwestern's projections and its actual experience, which in this case was a deficit. Transwestern sought to charge Williams and SoCal for these leftovers, even if both ceased buying gas from Transwestern altogether. Obviously there is no mootness objection here; if the charges are lawful, Transwestern will collect them. Finding the record unclear as to whether some portion of the charge may be barred by the filed rate doctrine, we remand to the Commission for its resolution of that issue.

Before 1972 pipelines based the gas cost component of their sales rates on a projection of their recent purchase prices into the future. Because of the rapid escalation of wellhead prices then under way, they were continually falling behind, and, to minimize their losses, frequently filed new rates under § 4 of the Natural Gas Act. To reduce this frequency, the Commission in 1972 promulgated a system for more direct tracking of purchase prices. As before, a pipeline would project historical prices into the future. But when its experience in the next six months differed from the projection (as presumably it always did), the difference was added to or subtracted from the rates for the next six months, in a so-called purchased gas adjustment or PGA. See Order No. 452, *Purchased Gas Cost Adjustment Provision in Natural Gas Pipeline Companies' FPC Gas Tariffs*, 47 FPC 1049, 1050-51 (1972); see also *Standard Form for Purchased Gas Adjustment Filings Submitted by Natural Gas Pipeline Companies*, Regulations Preambles [1982-1985], Stats. & Regs. ¶ 30,515 at 30,786; see generally 18 CFR §§ 154.301-154.310 (1989). The figures describing the difference between projection and experience were reflected in each pipeline's "Account No. 191."

As the certificate approved by the Commission here altogether dropped the system of projecting rates from past experience, the entire theory underlying the PGA and Account No. 191 became irrelevant. Transwestern, however, sought authority under which, if both customers nominated zero purchases under the new certificate, it could bill them any amounts remaining unrecovered in its Account No. 191 at the moment of transition (in proportion to their contract demand in the prior period). The Commission agreed. 43 FERC at 61,653.

The filed rate doctrine prohibits the Commission from imposing a rate different from the one on file at the time gas is sold or service made available. It allows purchasers of gas to know in advance the consequences of the pur-

chasing decisions they make, see *Columbia Gas Transmission Corp. v. FERC*, 831 F.2d 1135, 1141 (D.C. Cir. 1987) (quoting *Electrical District No. 1 v. FERC*, 774 F.2d 490, 493 (D.C. Cir. 1985), and extending it from the Commission's "fix[ing]" of rates under § 5 to its approval of rates filed under § 4 but imposed on purchasers in proportion to their prior gas purchases), although, as we shall see, a customer's ability to escape a charge may as a practical matter be seriously constrained despite the doctrine.

Our decisions on the necessary notice have not been altogether clear. In *Electrical District* the Commission sought to make a rate effective under § 5 as of the date it *ordered* the pipeline to make a compliance filing rather than the date on which the Commission *accepted* the compliance filing. Even though the purchasers of the electricity in that case could evidently have estimated with some precision the rates the compliance filing would impose, the court held that the Commission's attempt to make the new rate effective as of the earlier date violated the filed rate requirement because the purchasers did not know the "numerical rate" they would be charged. *Id.* at 492. The court recognized that specificity of notice is often a matter of degree but rejected as too amorphous a standard that would turn on such degrees. Instead it adopted a bright-line insistence that a numerical rate be "specified." *Id.* at 492-93; see also *Public Service Co. of New Mexico v. FERC*, 832 F.2d 1201, 1225 (10th Cir. 1987) (adopting rule of *Electrical District*).

On the other hand, in *Public Service Co. of New Hampshire v. FERC*, 600 F.2d 944 (D.C. Cir. 1979), the court addressed an electrical utility's ability to collect for costs that were left over as a result of transition from one billing system to another. It drew a distinction between "fixed rate" tariffs, charging a "predetermined price per unit based on costs incurred during some past test period, subject to some adjustments," and "cost of service"

tariffs, which as understood by the court precisely tracked actual fuel costs but which required "deferred billing." *Id.* at 948. Under the latter system, as evidently envisaged by the court, a customer would not know until (say) March the unit price due for January's usage; on billing, it would pay the then-revealed rate times the quantity taken.[4] While the court said that the rule against retroactive ratemaking would be no bar to collection of the leftovers if the outgoing system had been cost of service, it found that system to have been a fixed rate tariff, and therefore held the leftovers uncollectible. *Id.* at 950. Thus the court was clearly untroubled by a rate system under which a customer *could not* know the exact charge for service in a given period until after the end of the period. This is far less than what *Electrical District* viewed as the minimum.

But we think the two cases can be reconciled. The Commission need not confine rates to specific, absolute numbers but may approve a tariff containing a rate "formula" or a rate "rule" (as *Public Service Co. of New Hampshire* assumed); it may not, however, simply announce some formula and *later* reveal that the formula was to govern from the date of announcement (as it had done in *Electrical District*). We recognize that this view of *Electrical District* fails to implement its objective of eliminating the problems of drawing lines as to what notice is adequate, but we think that where the Commission explicitly adopts a formula and indicates when it will take effect, courts may not (without invading the Commission's province) say that such a formula may

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[4] In actual fact, the tariffs characterized by the court as "cost of service" appear *not* to have fit its description. The only description of such a tariff in the Commission brief is of the PGA system involved in *Transwestern*, under which the customer pays in one period a rate fixed for that period, with discrepancies corrected by adjustments in a later period's charge per unit. See Commission Brief at 30-31 in *Public Service Co. of New Hampshire*, 3076 Records & Briefs U.S. Court of Appeals (D.C.).

never qualify as a "rate" within the meaning of § 4 or § 5 of the Natural Gas Act. See *Chevron USA, Inc. v. Natural Resources Defense Council*, 467 U.S. 837 (1984).

Moreover, this approach is a natural corollary of the rule that *Electrical District*'s insistence on absolute precision does not apply where the parties have *agreed* that rates shall take effect before their exact formulation. See *Panhandle Eastern Pipe Line Co. v. FERC*, 881 F.2d 1101, 1120-21 (D.C. Cir. 1989) (rejecting argument that *Electrical District* trumps parties' agreement to the contrary); see also *Public Service Co. v. FERC*, 851 F.2d 1548, 1556-57 (5th Cir. 1988) (same).[5] A tariff that is filed under § 4 and accepted by the Commission is itself a kind of substituted contract—with the Commission acting as a referee of the competing interests (customers, pipelines), making sure that the utility's monopoly power does not bring about rates that are materially worse for the customers than what they could get for themselves under competition.

Here the Commission by order of May 11, 1988 approved Transwestern's proposed certificate, with its provision for disposition of Account No. 191 balances.

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[5] The rule of *Electrical District* also does not apply when the refund provisions of § 4 of the Natural Gas Act are triggered, or when the Commission commits a legal error that unlawfully delays the time as of which it establishes a corrected rate under § 5, 15 U.S.C. § 717d. See *Office of Consumers' Counsel v. FERC*, 826 F.2d 1136, 1138-39 (D.C. Cir. 1987); *Tennessee Valley Mun. Gas Ass'n v. FPC*, 470 F.2d 446, 452-53 (D.C. Cir. 1972); see also *United Gas Improvement Co. v. Callery Properties, Inc.*, 382 U.S. 223, 229-30 (1965) (upholding Commission decision to order refunds on rates where original Commission approval under § 7 of the Act was judicially found unlawful). In *Office of Consumers' Counsel*, for example, the court held that where the Commission found practices unlawful under § 5 but wrongly denied relief, new rates prescribed as a result of court correction of the error could be effective as of the date of the Commission's finding of unlawfulness. No one suggests that these exceptions relating to correction of Commission error are applicable here.

It provided that if SoCal nominated zero (the Commission was already aware of Williams's zero nomination), the balance remaining in Account No. 191 would be divided between the customers in accordance with their respective contract entitlements (85.7% for SoCal and 14.3% for Williams). 43 FERC at 61,653.

The downstream purchasers note that as matters worked out, this put SoCal in a difficult position. Since Williams opted out on February 1, 1988, SoCal knew that under the May 11, 1988 order it would bear either the whole charge (if it elected any sales service) or its proportionate amount (if it elected none), "two unappealing options." Downstream purchasers' Initial Brief at 14. That options may be unappealing, however, does not make the Commission's presentation of them an automatic violation of the filed rate doctrine. In any event, the first of the options (SoCal bearing the whole charge if it continued to take sales service) was no more than what would have happened under the existing PGA regulations, before the new Transwestern filing, under the same circumstances. See *Kentucky West Virginia Gas Co.*, 37 FERC ¶ 61,310 (1986), reh'g denied, 44 FERC ¶ 61,044 (1988), appealed, Nos. 88-4463 (5th Cir.) and 88-3820 (6th Cir.).

As to Williams, the Commission's position is more difficult. First, Williams elected on February 1, 1988 to end its purchase entitlements effective February 1, 1989, so that it had cast its die before the Commission's May 11, 1988 statement of the consequences. Nonetheless, it continued to be the beneficiary of its contract entitlement from May 11, 1988 until February 1, 1989, and its actual takes of gas in that period played a role in determining the size of the Account No. 191 balance. That Williams could have avoided the charge only by accelerating the abandonment of service—an avenue that was probably not open to it as a practical matter—does not make the charge a violation of the filed rate doctrine. All adjust-

ments in fixed charges after the customer first joins the system, i.e., in all charges not directly correlated with actual takes (such as a commodity charge), suffer from that feature. In so far as prior discussions in our cases have suggested that a rate violates the filed rate doctrine simply because a customer cannot respond in some way that enables it to escape the charge, see e.g., *Columbia Gas*, 831 F.2d at 1141 (quoting *Electrical District*, 774 F.2d at 493); see also *Associated Gas Distributors v. FERC*, 893 F.2d 349, 356-57 (D.C. Cir. 1989), such remarks were clearly inconsistent with the acknowledged power of the Commission to establish, and to alter prospectively, fixed charges such as demand charges, avoidable if at all only through the elaborate process of securing abandonment under § 7 of the Act.

Account No. 191 balances accrued after the termination of Williams's purchase entitlements on February 1, 1989 pose another problem. In that period it neither received nor was entitled to receive service. We can see little sense in such a charge; it certainly violates the Commission's policy of attempting to match revenues from each class of customers with their respective responsibility for costs. See, e.g., *Alabama Electric Cooperative, Inc. v. FERC*, 684 F.2d 20, 27 (D.C. Cir. 1982). But no one has attacked the Commission's treatment of the PGA balance on that basis, before us or on rehearing before the Commission, so we have no jurisdiction to consider the matter. See § 19 of the Act, 15 U.S.C. § 717r. In sum, then, we see no obstacle under the filed rate doctrine to Transwestern's collection of Account No. 191 balances accrued after the May 11, 1988 order.

It appears, however, that some portion of the PGA balances remaining at June 30, 1989 may have accrued before May 11, 1988. Commission Brief at 63 n.44. Accordingly we must examine the Commission's contentions that it had previously made clear that the balances would be collectible against departing customers if all jumped

ship. The prior occasions consist of its promulgation of the PGA regulations themselves and two 1986 decisions, relating to other pipelines, in which it allowed catch-up of the balances. We reject both theories.

Under the PGA regulations, a customer who leaves the system is normally no longer responsible for any adjustment costs. See *Kentucky West Virginia Gas Co.*, 37 FERC at 61,912.[6] But the Commission argues that because its preamble to the regulations asserted the purpose of "assur[ing] [pipelines] the recovery of all purchased gas costs," Order No. 452, 47 FPC 1049, 1051, modified, 47 FPC 1510 (1972), modified, 49 FPC 84 (1973), Transwestern's customers had notice since 1972 that these balances would follow them if the PGA system ended altogether. We find these expressions of PGA purposes inadequate to such a task. The scenarios of multiple departures, culminating in a complete end of PGA sales, are varied and complex, and there are other policy values that a customer might think would also bear upon the Commission's resolution of such an issue. Suppose, for instance, each of 20 customers left a system seriatim, the last accounting only for 5% of the pipelines' sales. Would the Commission policy in favor of assuring pipelines' full recovery of costs trump its policy in favor of having prices track responsibility for costs? Where circumstances suggest many approaches to a problem and many values requiring consideration, the Commission's assertion of a policy goal in one context is hardly the same as a rule implementing that goal in every other context.

The Commission also would have us find notice in two 1986 decisions. In *Western Gas Interstate Co.*, 34 FERC ¶ 61,122, reh'g denied in part, 35 FERC ¶ 61,012 (1986), the Commission allowed a pipeline to bill its sole remain-

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[6] Conversely, any new customer can reap the benefit of an overcharge in a previous period even though the customer in no way contributed to the surplus. 37 FERC at 61,914 n.8.

ing customer the balance of its Account No. 191 after it received authority to abandon the relevant service. 34 FERC at 61,197; see also 35 FERC at 61,020 (Order on Rehearing). In *Locust Ridge Co.*, 37 FERC ¶ 61,295 (1986), the Commission also allowed a pipeline terminating its PGA filings to "refund or direct bill the remaining balance" in its Account No. 191. 37 FERC at 61,883. Since these cases did not involve Transwestern's system, they could provide notice only in the sense of representing the state of FERC law interpreting the earlier PGA regulations.

Both of the decisions are quite summary and lack any analysis of the issue. Neither purports to lay down any sort of general rule for the treatment of Account No. 191 balances on complete termination of service. When FERC disallowed recapture by direct billing against a *single* departing customer, in *Kentucky West Virginia Gas Co.*, it relied not only on the pipeline's ability to collect the deficiencies from remaining customers but also on its finding that customers had inadequate notice that they would be charged for these costs. While *now* FERC explains that the first point was controlling, see Commission Brief at 61 n.41, *Kentucky West Virginia* did not say so, and did not even mention the earlier brief orders allowing direct billing. Even if *Kentucky West Virginia* is ultimately reconcilable with *Locust Ridge* and *Western Gas*, we can hardly impute adequate notice to Transwestern's customers merely because their lawyers, if put to work on the problem, might have divined a theory reconciling the cases.[7]

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[7] As a last stand, FERC argues that its power to waive the thirty-day notice requirement under § 4(d) of the Natural Gas Act somehow translates into a power to waive the filed rate doctrine altogether. See *Transwestern Pipeline Co.*, 44 FERC ¶ 61,164 at 61,537 (1988) (order on rehearing). Given our conclusion that the filed rate doctrine is no bar to Transwestern's collection of unrecovered purchased gas costs incurred after May 11, 1988, this argument only applies to costs in Account No. 191 which were incurred prior to that date. Whatever remaining life this claim might otherwise have

Finding no meaningful notice in any Commission act before May 11, 1988, we remand the case to the Commission for it to determine what portion of the Account No. 191 deficiency accrued thereafter.

Transwestern's Attack on the Commission's Redocketing its § 4 Filing with its § 7 Filing

It will be recalled that Transwestern filed its new rate proposals, including its gas inventory charge, under § 4, together with a companion filing under § 7 for an amendment to its certificates such that a nomination below a customer's certificated entitlement would result in abandonment of the excess. Viewing the two as inextricably linked, the Commission rejected the § 4 filing and redocketed it under § 7. See *supra*, at 9-10. Thus, says Transwestern, the Commission delayed the time as of which it could secure the benefit of the new rates.

We find the claim as moot as the downstream purchasers' objections to the Commission's approval of the Transwestern rate scheme, and for the same reasons. As a result of Williams's and SoCal's zero nominations, no rates have ever been or will ever be charged under the Commission decision.[8] Had the Commission accepted Transwestern's § 4 filing as such, its customers would simply have been forced to decide earlier whether to terminate their sales service with Transwestern. Transwestern has offered no basis for believing that an earlier effective date would have resulted in positive nominations. The sole respect in which Transwestern's rates would have been more attractive independently of the § 7 filing is that nominations lower than firm sales entitlement

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here, it was recently rejected by another panel of this circuit. See *Columbia Gas Transmission Corp. v. FERC*, 895 F.2d 791 (D.C. Cir. 1990).

[8] Transwestern does not claim that the Commission's decision to redocket the § 4 filing prejudiced it with respect to its collection of the remaining Account No. 191 balance.

would not have immediately triggered abandonment, but in view of the § 7 filing, customers deciding on nominations presumably would have considered the prospect of Commission approval. It is speculative in the extreme to suggest that this shadowy distinction would have produced different results.

Transwestern's Attack on Conditions Attached to the Certificate

The Commission subjected Transwestern's proposed certificate to two conditions. Transwestern objects, but we find its objection to the first moot and we find Transwestern not aggrieved by the second condition within the meaning of § 19(b), 15 U.S.C. § 717r(b).

First, FERC prohibited Transwestern from charging SoCal an "exit fee" in the event that it nominated no sales service under the certificate. See 43 FERC ¶ 61,240 at 61,654. No one has pointed us to anything in Transwestern's filings *proposing* an exit fee that would have applied to *initial* zero purchase decisions, and in any event, in Transwestern's petition for rehearing it challenged only the Commission's prohibiting it from "assess[ing] an exit fee if Southern California first commits to purchases under the GIC and *subsequently* reduces its nominations." 44 FERC at 61,536 (emphasis added); see also *id.* at 61,535. As this scenario cannot occur, the issue is moot.

In its second condition, the Commission prohibited Transwestern, after *acceptance* of the certificate, from "recover[ing] take-or-pay prepayment, buyout or buydown costs incurred after the date this certificate is accepted other than through the GIC mechanism." 43 FERC at 61,658. It distinguished between those costs and "costs that have already been paid or which are known and measureable through reference to binding written agreements entered into before acceptance of the GIC certificate," 44 FERC at 61,535, the latter type being

still recoverable through the Order No. 500 "equitable sharing" despite the acceptance of a GIC certificate.

The Commission insists that a certificate condition appearing to bar a utility from proposing, or itself from accepting, a specified type of rate, does not in fact do so in the absence of special circumstances. In *Tennessee Gas Pipeline Co. v. FERC*, 689 F.2d 212, 214-15 (D.C. Cir. 1982), we upheld the Commission's attachment of a condition to a § 7 certificate that seemed to bar a specific type of rate filing under § 4 because we did not read the condition as actually precluding such a filing. We distinguished *Algonquin Gas Transmission Co. v. FPC*, 534 F.2d 952 (D.C. Cir. 1976), on the ground that there the Commission had already rejected a nonconforming § 4 filing because it felt bound by the earlier condition, making the permanency of the condition appear rock-solid. Here the condition as to take-or-pay recovery appears no more permanent than the one found unobjectionable in *Tennessee Gas.*

Even if Transwestern could reasonbly have read the condition as binding, its only potential loss appears to have been its inability to recover a greater share of its take-or-pay costs under the "equitable sharing" mechanism. In *Associated Gas Distributors v. FERC*, 893 F.2d 349 (D.C. Cir. 1989), however, we struck down the equitable sharing mechanism as a violation of the filed rate doctrine. *Id.* at 354-57. As a result, we now know that that avenue of recovery was foreclosed. With Transwestern free to make new, nonconforming proposals for recovery of take-or-pay costs of the type the Commission appeared to bar, we cannot find Transwestern aggrieved by the take-or-pay exclusivity provision as required for our jurisdiction under § 19(b) of the NGA.

Conclusion

We find the downstream purchasers' claim that the treatment of Transwestern's Account No. 191 balances violates the filed rate requirement valid only in so far as those balances were accrued before May 11, 1988, and remand the case for making any necessary adjustment; we dismiss their other objections as moot. We reject on the merits Transwestern's claim that the Commission should have accepted its 1986 filing, we dismiss as moot its objections both to the Commission's coalescing of its 1987 § 4 and § 7 filings and to the imposition of an exit fee prohibition, and we find it not aggrieved by the take-or-pay exclusivity condition.

So ordered.

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 88-1046

TRANSWESTERN PIPELINE COMPANY,
Petitioner

v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent

and Consolidated Cases

Before: Williams, D. H. Ginsburg and Sentelle, Circuit Judges

ORDER

[Filed May 31, 1990]

Upon consideration of the petitions for rehearing of the respondent Commission and petitioner Transwestern Pipeline Company, it is

ORDERED, by the Court, that the petitions are denied. Neither the Commission nor Transwestern raised in their briefs the argument that Transwestern's filing in December 1987 gave notice that the customers would be charged the remaining balance in Account No. 191 in the event all customers left the system. We therefore did not and do not address it. See *Carducci* v. *Regan*, 714 F.2d 171, 177 (D.C. Cir. 1983).

Per Curiam

FOR THE COURT:
CONSTANCE L. DUPRE
Clerk

By: /s/ Robert A. Bonner
ROBERT A. BONNER
Deputy Clerk

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 88-1046

TRANSWESTERN PIPELINE COMPANY,
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v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent

and Consolidated Cases

Before: Wald, Chief Judge; Mikva, Edwards, Ruth B. Ginsburg, Silberman, Buckley, Williams, D. H. Ginsburg, Sentelle and Thomas, Circuit Judges

ORDER

[Filed May 31, 1990]

The Suggestions For Rehearing *En Banc* of the respondent Commission and petitioner Transwestern Pipeline Company have been circulated to the full Court. No member of the Court requested the taking of a vote thereon. Upon consideration of the foregoing it is

ORDERED, by the Court *en banc*, that the suggestions are denied.

Per Curiam

FOR THE COURT:
CONSTANCE L. DUPRE
Clerk

By: /s/ Robert A. Bonner
ROBERT A. BONNER
Deputy Clerk

A statement of Chief Judge Wald is attached.

Separate statement of Chief Judge Wald—No. 88-1046, *et al.*

I would ordinarily call for a vote on the suggestion for rehearing *en banc*. As I noted in my dissent from the denial of the petition to rehear *en banc AGD v. FERC*, No. 88-1385 (March 30, 1990), I think the Court's current interpretation of the filed rate doctrine is overly rigid, at a time when the FERC needs latitude to navigate the recent dramatic changes in the structure of the natural gas industry. However, the decisive vote against rehearing *en banc* in *AGD v. FERC* convinces me that to call for a vote for rehearing *en banc* in this case would be equally futile. It remains for the Supreme Court to settle this important question of how impenetrable a barrier the filed rate doctrine is to FERC's efforts at allocating the inevitable burdens stemming from fundamental readjustment of the pipeline industry.

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 88-1046

TRANSWESTERN PIPELINE COMPANY,
Petitioner

v.

FEDERAL ENERGY REGULATORY COMMISSION,
Respondent

and Consolidated Cases

Before: Williams, D. H. Ginsburg and Sentelle, Circuit Judges

ORDER

[Filed Jun. 27, 1990]

Upon consideration of the motions for stay of mandate, it is

ORDERED, by the Court, that the motions are granted and the Clerk is directed to withhold issuance of the court's mandate for a period of sixty days from the date of this order.

Per Curiam
FOR THE COURT:
CONSTANCE L. DUPRE
Clerk

By: /s/ Robert A. Bonner
ROBERT A. BONNER
Deputy Clerk

FEDERAL ENERGY REGULATORY COMMISSION

Docket Nos. RP88-35-000, CP88-99-000,
CP88-100-000, and CP88-143-000

TRANSWESTERN PIPELINE COMPANY

ORDER REDOCKETING FILING, CONSOLIDATING DOCKETS, GRANTING MOTIONS TO INTERVENE, AND CONVENING TECHNICAL CONFERENCE

(Issued December 31, 1987)

Before Commissioners: Martha O. Hesse, Chairman; Anthony G. Sousa, Charles G. Stalon, Charles A. Trabandt and C. M. Naeve.

On December 1, 1987, Transwestern Pipeline Company (Transwestern) filed three interrelated filings with the Federal Energy Regulatory Commission (Commission): (1) proposed tariff sheets which would allow customers served under Transwestern's Rate Schedules CDQ-1 and CDQ-3 to nominate a desired level of sales service;[1] (2) an application for pre-granted permission and approval to abandon existing firm CDQ sales service to the extent customer nominations are lower than existing CDQ sales entitlements;[2] and (3) an abbreviated application for permanent blanket certificate authority to implement an off-system and on-system interruptible sales service and

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[1] This filing was docketed in Docket No. RP88-35-000.

[2] The Commission is considering this second filing in Docket No. CP88-99-000.

for pre-granted abandonment to terminate such services.[3] Because of the interrelationship of these filings, the Commission is consolidating them for simultaneous evaluation.

Transwestern's Proposal

Transwestern filed proposed tariff sheets seeking authority to establish a Gas Supply Inventory Charge (GIC) to become a permanent part of its tariff (GIC filing). Transwestern states that its GIC filing fulfills the requirements of each of the principles outlined for such a charge in Section 2.105 of the regulations, promulgated by Order No. 500.[4]

Transwestern proposes to allow its customers to freely nominate their desired level of Contract Demand Quantity (CDQ) under Rate Schedules CDQ-1 and CDQ-3 up to the level of their presently certificated level of contract demand quantities. Prior to its customers' annual nominations, Transwestern would provide a schedule of gas purchase costs which would depict gas prices at various purchase levels to which Transwestern would commit to be in effect during the period its customers' nominations were to be in effect. To the extent the customers' aggregate existing firm sales entitlements exceed 367,500 dth per day, the customers would be given the additional option of submitting revised nominations based upon a revised schedule of gas costs to be incurred for the upcoming quarter for volumes in excess of 367,500 dth per day. Any time a customer were to reduce its nominated level of CDQ, the difference between the previous nomination and the reduced nomination would be abandoned. The GIC would be applicable to daily volumes nominated but not purchased and would be the only means Trans-

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[3] The Commission is considering this third filing in Docket No. CP88-100-000.

[4] Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol, Docket No. RM87-34-000, Order No. 500, Interim Rule and Statement of Policy, 52 Fed. Reg. 30,334 (Aug. 14, 1987), *FERC Statutes and Regulations* ¶ 30,761 (1987).

western would employ to collect take-or-pay costs attributable to the period during which the GIC is in effect.[5] The GIC rates also would be provided to Transwestern's customers prior to any permitted nominations. According to Transwestern, this would enable them to know both the costs associated with the service to be nominated as well as the cost consequences of purchasing gas at levels below their currently effective nominated levels of CDQ.

Transwestern proposes that small-volume customers served under Rate Schedules SG-1, SG-2 and RW-1 would be charged rates based upon a gas cost component determined by the nomination levels of Transwestern's CDQ-1 and CDQ-3 customers.

Transwestern proposes to suspend its PGA during the period the GIC is in effect. Within 60 days following July 1, 1988, the effective date of initial nominations under the GIC proposal, Transwestern would bill or refund each CDQ customer's proportionate share of any amounts accumulated in its Unrecovered Purchased Gas Account (FERC Account No. 191) as of June 30, 1988. Similarly, Transwestern would bill or refund at six-month intervals the amounts which accumulate in FERC Account No. 191 subsequent to the effective date of the GIC which reflect gas costs for any period prior to such date. However, Transwestern seeks to reserve the right to reinstate its PGA on 30 days notice.

Transwestern proposes a January 1, 1988 effective date for the above tariff sheets.

Interventions and Protests

On December 7, 1987, the Commission issued a notice in Docket No. RP88-35-000 of Transwestern's proposed

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[5] Transwestern states that costs incurred to buy out or buy down existing contracts to make them more market-responsive may be included in a later filing.

tariff sheets.[6] In response, the Commission received 21 timely motions to intervene,[7] four protests,[8] and four requests for hearing.[9] None of the interventions is opposed, consequently, pursuant to Rule 214, 18 C.F.R. § 385.214, all of these intervention motions are granted. Texas Eastern Transmission Corporation filed a late motion to intervene which also will be granted.

The Kansas Corporation Commission expresses concern that Transwestern's proposed GIC could result in large expenses being assessed against Williams Natural Gas Company, a major gas supplier in Kansas, and that Williams would seek to recover these expenses in its rates for service in Kansas.

Kansas Power and Light Company (KP&L) argues that Transwestern's forward supply service is in essence a minimum take and pay requirement which the Commission subsequently rejected as unlawful in Opinion No. 238[10] and *Transwestern Pipeline Co.*,[11] and which

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[6] 52 Fed. Reg. 47,046 (December 11, 1987). The tariff sheets at issue are listed in Appendix A to this order.

[7] Mock Resources, Inc., El Paso Natural Gas Company, Southwest Gas Corporation, the Public Utilities Commission of the State of California (California, PUC), Chevron U.S.A., Inc., Kansas Power and Light Company (KP&L), Natural Gas Clearinghouse, Inc., Phelps Dodge Corporation, Producer Associations, Salt River Project Agricultural Improvement and Power District, Arizona Public Service Company, Tenneco Oil Company, Columbia Gas Transmission Corporation, Hadson Gas Systems, Inc., Southern Union Gas Company, Tennessee Gas Pipeline Company, Williams Natural Gas Company, the State Corporation Commission of the State of Kansas (KCC), Arco Oil and Gas Company, Southern California Gas Company (SoCal), and Pacific Gas and Light Company.

[8] California PUC, SoCal, KCC, and KP&L. The Commission construes KP&L's motion for summary rejection to be a protest.

[9] California PUC, SoCal, KCC and KP&L.

[10] 32 FERC ¶ 61,009 (1985).

[11] 32 FERC ¶ 61,310 (1985).

the Commission in Order No. 380-C declared unreasonable under the Natural Gas Act.[12] KP&L also contends that Transwestern's forward supply service fails to constitute an advance commitment to specific "posted rates" as discussed in Appendix A to Order No. 500.[13] According to KP&L, the forward supply service is even more onerous and anti-competitive than Transwestern's minimum bill requirements which the Commission has already rejected, in that it contains no make-up rights and imposes a penalty if the buyer purchases less than 100 percent of the minimum gas quantity. Moreover, KP&L complains that Transwestern's proposal would permit the pipeline to recover from its customers all its take-or-pay buyout costs, in contravention of Order No. 500's requirement that pipelines bear a portion of such costs. Finally, KP&L argues that the GICs are not cost-based and therefore do not qualify as just and reasonable under the Natural Gas Act.

The California Public Utility Commission argues that (i) the minimum take-and-pay requirement in Transwestern's proposal contravenes the Commission's ruling in Order No. 380-C (referred to above); (ii) Transwestern's proposal failed to alter the curtailment provisions of its tariff to ensure that Transwestern's customers would have a contractual right to recover damages from Transwestern in the event that gas for which a reservation charge has been paid is not delivered or is otherwise unavailable; (iii) the gas prices are not cost-based and are therefore not just and reasonable; (iv) the proposal does not provide for crediting the take-or-pay relief which Transwestern will obtain when it sells gas abandoned under the proposal; (v) the GIC is arbitrarily based on an unsubstantiated assumption that all take-or-pay liabilities will be settled for 25 cents on the dollar; (vi) the

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[12] *FERC Statutes and Regulations, Regulations Preambles 1982-1985* ¶ 30,607, at p. 31,187 (1984).

[13] *FERC Statutes and Regulations* ¶ 30,761, at p. 30,803 (1987).

proposal does not give Transwestern's customers the right to automatic reinstatement of their contract demand quantities without a minimum bill restriction in the event that Transwestern terminates open access transportation; and (vii) the proposal is inconsistent with Order No. 483 to the extent that it provides for reinstatement of Transwestern PGA provisions on 30 days notice.

Southern California Gas Company contends that (i) the proposal fails to provide a firm price or pricing formula as required in § 2.105 of the Commission's regulations; (ii) the proposal's reservation of the right to reinstate a PGA on 30 days notice violates the revised PGA regulations instituted in Order No. 483; (iii) the proposal's forward gas supply service provisions violate Order No. 380's prohibition of minimum bills; (iv) the proposed rates are not cost-based and are overstated; and (v) the proposed GIC mechanism is also not cost-based.

The Commission will direct the staff to convene a technical conference to explore the basis for these protests, as well as other issues, discussed below, that are raised by the GIC filing.

Discussion

Transwestern's proposal results in fundamental changes in the service relationship between the pipeline and its customers. If the customer nominates less than its contract demand level, the customer releases Transwestern from its obligation to supply above the nominated level. This, coupled with Transwestern's request for pre-granted abandonment in Docket No. CP88-99-000 constitutes a significant change in the service relationship between the pipeline and its customers and requires an amendment to the existing sales certificates to service those customers. This is not the kind of change in service that can or should occur without the Commission first deciding whether the change satisfies the public interest standards in Section 7(c) of the Natural Gas Act. Treating Trans-

western's GIC proposal as a change in service, necessiating a certificate amendment, is consistent with the Commission's treatment of similar gas inventory proposals.[14]

In order to place this proceeding in the posture which the Commission thinks is the correct one, the Commission shall redocket Transwestern's filing from Docket No. RP88-35-000 to Docket No. CP88-143-000, and treat it as an application for a certificate amendment.[15] Therefore, the tariff sheets filed in Docket No. RP88-35-000 will not be accepted for filing at this time, but will be held as *pro forma* sheets for evaluation in the certificate proceeding.

Transwestern has proposed a "market-based" GIC, in which the level of the inventory charge would be established by the market. In support of this proposal Transwestern has provided information to show that its markets are competitive. While Transwestern's filing goes a long way toward establishing the competitiveness of its markets, at least with respect to its largest customers, additional factors need to be explored through the technical conference that is to be convened by the staff. For example, the question should be explored of customer access to alternative supplies and whether adequate alternative supplies, not under contract to Transwestern and connected to Transwestern's system, are available, or will be available, to Transwestern's customers.

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[14] *See, e.g., Natural Gas Pipeline Co. of America,* Docket No. RP87-141-000 *et al.,* Order Modifying and Partially Vacating Prior Order, Partially Granting and Denying Requests for Rehearing and Clarification, and Dismissing Protests, slip op. at 3-4 (December 28, 1987) [41 FERC ¶ 61,358]; *Texas Eastern Transmission Corp.,* Docket No. RP85-177-044, *et al.,* Order Accepting Compliance Filing, Subject to Conditions, and Establishing Hearing Procedures, slip op. at 13 (December 31, 1987) [41 FERC ¶ 61,373].

[15] Transwestern's previously paid filing fee will be credited toward payment of the filing fee for a certificate amendment.

Other issues to be explored at the technical conference include the following: The appropriateness of Transwestern being able to abandon its GIC and reinstate its PGA merely by giving 30 days notice of its decision to exercise that option. Among other things, the Commission questions whether this would be consistent with the fact that Transwestern must hold its stated price for the stated period. Transwestern's proposal uses aggregate customer purchases to determine the price that all customers will pay on a given day. As a result, an individual customer may not know with certainty its cost of gas in advance, since the aggregate purchases would only be known after the fact. In addition, the cost of gas to be paid by the customers would vary indirectly with the volumes purchased so that as the volumes purchased increase, the price will decrease. This rate structure would appear to bias customer nominations by creating an incentive for customers to either nominate high or zero volumes. Also, the cost of gas to be paid by the small Rate Schedule SG and RW customers would appear to be determined solely by the nominations of the large customers. These issues, as well as the basis for the protests of the intervenors should be explored at the conference. As a result of the staff report the Commission will be in a better position to determine whether further procedural steps may be necessary.

The Commission orders:

(A) The tariff sheets filed in Docket No. RP88-35-000 are not accepted for filing at this time. This tariff sheets reflecting the GIC, listed in Appendix A to this order, will be held as *pro forma* sheets, to be considered in Docket No. CP88-143-000.

(B) The proceedings in Docket No. RP88-35-000 are redocketed as Docket No. CP88-143,000 and Docket Nos. CP88-99-000, CP88-100-000 and CP88-143-000 are consolidated.

(C) All motions to intervene in Docket No. RP88-35-000 are granted and all intervenors in any of the above captioned dockets, are deemed to be parties to the consolidated proceeding.

(D) The Commission staff is directed to convene a technical conference in the consolidated proceedings within 30 days of this order and within 60 thereafter the staff shall submit a report of the conference to the Commission.

Commissioner Stalon *dissented* in part with a separate statement.

APPENDIX A

Tariff Sheets Proposed To Be Effective
January 1, 1987

Second Revised Volume No. 1

Commissioner STALON, dissenting in part:

In this docket Transwestern Pipeline Company is seeking to establish a market-based gas inventory charge. As the Commission's order points out, the filing raises important questions concerning the competitiveness of Transwestern's markets, particularly the markets of small customers. These issues should not be left to a technical conference to resolve. The Commission has a responsibility to develop the issues raised by this filing in a hearing where a record can be fully developed.

FEDERAL ENERGY REGULATORY COMMISSION

Docket Nos. RP88-35-001, CP88-99-000,
CP88-100-000 and CP88-143-001

TRANSWESTERN PIPELINE COMPANY

ORDER DENYING REHEARING

(Issued March 25, 1988)

Before Commissioners: Martha O. Heese, Chairman; Anthony G. Sousa, Charles G. Stalon, Charles A. Trabandt and C. M. Naeve.

On December 31, 1987, the Commission issued an order [1] which, *inter alia*, declined to accept under section 4 of the Natural Gas Act certain tariff sheets filed on December 1, 1987 by Transwestern Pipeline Company (Transwestern) which provided for a Gas Supply Inventory Charge (GIC).[2] The Commission found that the GIC proposal would result in fundamental changes in the service relationship between Transwestern and its customers and therefore required a certificate amendment under section 7. Transwestern's GIC filing was redocketed as Docket No. CP88-143-000 and the tariff sheets reflecting the GIC were held for consideration as pro forma sheets in this latter proceeding. The Commission's December 31, 1987 order also consolidated the GIC proposal with two other certificate applications simultaneously filed by Transwestern in Docket Nos. CP88-99-000 and CP88-100-000. In Docket No. CP88-99-000, Trans-

[1] 41 FERC ¶ 61,371 (1987).

[2] Transwestern's GIC proposal was initially docketed in Docket No. RP88-35-000.

western seeks pre-granted abandonment of existing firm sales service to the extent such sales exceed customer nominations under the GIC proposal. In Docket No. CP-88-100-000, Transwestern seeks permanent general certificate authority to implement an off-system and on-system interruptible sales service and for pre-granted abandonment authority to terminate this service.

On January 29, 1988, Transwestern filed a request for rehearing of the Commission's December 31, 1987 order. It argues that the Commission erred in finding that implementation of the GIC would fundamentally change its service relationship with its customers. Transwestern contends that, in contrast, the Commission already authorized the services underlying the proposed GIC and that the GIC filing was made in response to the Commission's own instructions. Transwestern's rehearing request will be denied for the reasons set forth below.

Background

1. Transwestern's transportation settlement and standby charge

On July 30, 1985, Transwestern filed for a rate increase under section 4 and by order issued August 29, 1985,[3] the Commission accepted the filing, subject to refund and conditions. On January 16, 1986, Transwestern filed an offer of settlement which proposed to resolve all issues in that proceeding. Under the terms of the settlement, Transwestern agreed to become an open access transporter in accordance with the Commission's regulations at Part 284 [4] and to file for a blanket transportation certificate under section 284.221 of the Commission's regulations.[5] Under the terms of the settlement, Transwest-

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[3] 32 FERC ¶ 61,310 (1985) (Docket No. RP85-178-000.

[4] 18 C.F.R. Part 284 (1987).

[5] 18 C.F.R. § 284.221(a) (1987). Transwestern filed for its blanket certificate on December 17, 1987, and by order issued March 1, 1988, its proposal was approved. 42 FERC ¶ 62,187 (1988).

ern agreed, as required by the regulations, to provide firm sales customers the option to convert to firm transportation up to the level of their contract demand (CD) entitlements.[6]

The Commission's regulations permit, but do not require a pipeline to abandon sales service to the extent of the conversion.[7] The pipeline may instead choose to retain its section 7 sales certificate in order to stand ready to again provide sales service in the event the customer converts back to firm sales.[8] In the settlement, Transwestern agreed to provide this standby sales service and the Commission affirmed its right to do so, over the objections of certain producers that had been granted late intervention.[9] The Commission noted, however, that Transwestern's tariff lacked a charge to recover the costs associated with facilities and gas supplies necessary to provide sales in lieu of transportation service. As a condition to approval of the settlement, we required Transwestern, *inter alia*, to modify its tariff to include a standby charge.[10] On rehearing, however, we removed the standby charge requirement because: (1) Transwestern's rates, as designed, already allowed recovery of its costs; (2) no cross-subsidization of sales by transportation would result; and (3) the parties to the settlement had freely bargained for service without the standby charge.[11] Trans-

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[6] *See* 18 C.F.R. § 284.10(c). Under the terms of the settlement, the CD of Transwestern's principal customer, Southern California Gas Company (SoCal) was left unchanged under Rate Schedule CDQ-1 at 763,281 Dth per day. The CD of Williams Natural Gas Company (previously Northwest Central Pipeline Corporation) (Williams) under Rate Schedule CDQ-3 was reduced to 127,214 Dth per day, and its CD under Rate Schedule CDQ-2 was eliminated.

[7] 18 C.F.R. § 284.10(d) (1987).

[8] 50 Fed. Reg. at 42,443.

[9] 38 FERC at p. 61,169 (1987).

[10] *Id.* at p. 61,061.

[11] 41 FERC ¶ 61,178, at pp. 61,447-9 (1987).

western accepted the terms of the settlement as modified by the Commission's two orders addressing it and has continued to provide Part 284 transportation service under it.

2. Transwestern's direct billing proposal and supply reservation fee and the Order No. 500 guidelines

On June 12, 1986, during the pendency of the settlement proceeding noted above, Transwestern filed to revise its tariff to include a direct billing mechanism to recover certain payments it anticipated making to producers to waive or amend take-or-pay provisions in its gas supply contracts. Under this proposal, almost all of the take-or-pay buyout costs would have been borne by Transwestern's two principal CDQ customers, Williams and SoCal. The proposal also included a separate supply reservation charge to be paid to producers for receiving gas supplies in Transwestern's gas purchase contracts. The Commission rejected both the supply reservation charge and the direct billing mechanism.[12] With respect to the supply reservation charge, the Commission noted the subsequent issuance of Order No. 500 [13] on August 7, 1987, and the

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[12] By order issued July 11, 1986, at 36 FERC ¶ 61,048 (1986), the Commission rejected Transwestern's proposal without prejudice to its being raised at the hearing ordered therein. In an order issued May 8, 1987, at 39 FERC ¶ 63,025 (1987), the Administrative Law Judge (ALJ) found the direct billing proposal to be unjust and unreasonable and determined that the supply reservation charge was unnecessary in that no customer expressed a desire to avail itself of the backup or peaking service to which the charge would apply. *Id.*, at p. 65,131. By order issued September 28, 1987, at 40 FERC ¶ 61,324 (1987), *reh'g denied*, 41 FERC ¶ 61,235 (1987), the Commission affirmed the ALJ's rejection of the direct billing proposal on the grounds that it did not provide for the equitable sharing of costs between Transwestern and its customers. The Commission affirmed the ALJ's rejection of the supply reservation charge on the grounds that the record contained insufficient information to evaluate it properly. 40 FERC at pp. 61,995-6 (1987).

[13] *FERC Statutes and Regulations* ¶ 30,761 (1987). That order was modified in Order No. 500-A, *FERC Statutes and Regulations*

guidelines set forth therein for establishing mechanisms to recover costs of maintaining gas supplies for customers. The Commission suggested that Transwestern refer to them for guidance in the event it filed a revised proposal.[14] The guidelines in Order No. 500 are as follows:

> (1) The charge (which may not relate to facilities) is available to pipelines which transport gas under Part 284, of the Commission's regulations for standing ready to supply gas to sales customers;
>
> (2) The pipeline may not recover take-or-pay or similar charges from suppliers by any other means;
>
> (3) The pipeline must allow its customers to nominate levels of service freely within their firm sales entitlements or otherwise employ a mechanism for the renegotiation of levels of service at regular intervals;
>
> (4) The pipeline must announce in advance the price or pricing formula that will be in effect during the period for which nominations are being taken; and
>
> (5) The customer must consent to the abandonment of service for any difference between the nominated level of service and its previous firm sales entitlement.[15]

3. Transwestern's GIC proposal

As noted above, Transwestern submitted, on December 1, 1987, three interrelated filings, one of which proposed to establish a GIC in purported compliance with the fu-

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¶ 30,770 (1987), Order No. 500-B, *FERC Statutes and Regulations* ¶ 30,772 (1987), and Order No. 500-C, *FERC Statutes and Regulations* ¶ 30,786 (1987).

[14] 40 FERC at p. 61,995 (1987).

[15] *FERC Statutes and Regulations* ¶ 30,761, at p. 30,793 (1987), to be codified at 18 C.F.R. § 2.105.

ture gas supply guidelines. Transwestern proposed to suspend its PGA during the effectiveness of the GIC, subject to its reserved right to terminate the GIC and reinstate the PGA on 30 days' notice. The proposed effective date for the GIC mechanism was January 1, 1988, although the charge itself would not be billed until July 1, 1988.

In its December 31, 1987 order, the Commission observed that if a customer nominated less under the GIC than its existing CD entitlement, the customer releases Transwestern from its obligation to furnish gas above the new nomination level. The Commission found that this aspect of the GIC proposal, in conjunction with Transwestern's corresponding proposal in Docket No. CP88-99-000 for pre-granted approval to abandon CD entitlements above the new nomination level constituted a significant change in the service relationship between Transwestern and its customers and required a certificate amendment under section 7. The Commission also noted that the level of the GIC was proposed to be governed by market forces rather than by strict cost allocation principles. The Commission ordered that a technical conference be convened to examine the depth and extent of competition in Transwestern's markets and other issues raised by the filing.[16] Against this background we now evaluate Transwestern's contention on rehearing that its GIC proposal does not require a certificate amendment under section 7 but is properly viewed as a change in rates under section 4.

Transwestern's position

Before discussing the merits of Transwestern's rehearing request, it would be helpful at this juncture to summarize briefly its principal arguments. Transwestern contends that the Commission's approval of the standby charge in its open access settlement, in conjunction with

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[16] 41 FERC at p. 61,371 (1987).

the regulations at section 284.10(d),[17] which it asserts provide that a customer has consented to a pipeline's abandonment of firm sales entitlements to the extent that customer converts to firm transportation, provide all the regulatory approval necessary under section 7 for implementing its GIC. All that remains, in Transwestern's view, is the Commission's review of its GIC as a charging mechanism for previously considered and approved services. It recognizes that the Commission must approve the abandonment of its customers' CD entitlements in excess of their new nominations under the GIC, but argues that this abandonment is the subject of its separate, albeit related, application in Docket No. CP88-99-000. Transwestern argues that subjecting its proposal to certificate review under section 7, under which the Commission's final approval must be obtained prior to the collection of any charges, has created the potential for a confiscatory regulatory lag which would otherwise be delimited by the Commission's maximum five-month suspension power under section 4. Transwestern contends that this potential delay is tantamount to a retroactive conditioning of its certificate.

Discussion

1. Relationship of CD conversion regulations and Transwestern's open access settlement to its GIC proposal

Transwestern's central argument is that any fundamental changes requiring certificate authority under section 7 have already occurred and have been reviewed by the Commission, either in the context of the general rulemaking proceeding in Order No. 500 or as a result of the Commission's approval of its open access settlement. Transwestern contends that its GIC filing serves only as a means of recovering the cost of providing these previously approved services and that no further review under section 7 is required.

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[17] 18 C.F.R. § 284.10(d)(1)-(3) (1987).

Transwestern appears to argue [18] that the Commission's approval of its transportation settlement constitutes authority for it to implement its GIC. However, the standby service approved in the settlement is significantly different from that sought in the GIC. Moreover, in the settlement, the standby service arose out of Transwestern's election *not* to seek abandonment of that portion of its customers' CD entitlements converted to firm transportation, whereas here, a necessary part of Transwestern's GIC proposal is the abandonment of its existing standby service.

The standby service being provided is Transwestern's agreement to stand ready to provide, up to a customer's CD entitlement, sales service in the event the customer decides to swing back from transportation to sales. Thus, under the standby service, Transwestern's customers can choose between firm transportation and firm sales on a daily basis throughout the year. The GIC proposes to eliminate this dual capability for all practical purposes. If the GIC is adopted, a customer would be able to obtain only sales service under Transwestern's CDQ rate schedule. Any transportation service it desired would be provided under a new rate schedule.

Since the GIC envisions the discontinuance of its former standby service, Transwestern's argument is illogical and contradictory. Further, its GIC is not, as Transwestern argues,[19] merely a provision to recover costs of

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[18] Request for rehearing at 24-25.

[19] Request for rehearing at 15, 22 and 27. Transwestern also alleges that the Commission ordered or instructed it to file its GIC proposal. Request for rehearing at 15 and 22. This is incorrect. In the transportation settlement proceeding, the Commission acquiesced to Transwestern's own request not to impose a charge for its standby service. In the direct billing proceeding, the Commission merely suggested that Transwestern follow the Order No. 500 guidelines in any GIC proposal it chose to file. See discussion at n.n. 11 and 14, supra.

its previously approved standby service. As the Commission found on rehearing in the settlement proceeding, Transwestern's costs were already fully recovered in its stated rates at design throughput, thereby eliminating the need for assessment of a separate standby charge to its sales customers.[20] Thus, Transwestern's characterization of the GIC as a necessary charging mechanism for its existing standby service is erroneous. As the above discussion clearly demonstrates, the sales rate schedule including the GIC is a substantially changed service incorporating a new cost recovery mechanism. Unlike the existing standby service, the GIC would charge sales customers for not taking gas at the level of their GIC nominations.

Transwestern also appears to argue[21] that to the extent its proposed GIC requires authority to abandon sales service, that authority already exists under section 284.10 (d) of the regulations. It focuses on the parallel between the last guideline in Order No. 500, which provides that in reducing its sales service nomination below its existing CD entitlement, a customer would be consenting to any abandonment sought by a pipeline for the decrease, and the provisions of section 284.10(d), which provide for the filing by the pipeline of an application under section 157.18[22] of the regulations for abandonment of sales service to the extent a customer converts its firm CD entitlement to firm transportation. Under section 284.10(d)(3), the abandonment of sales service converted to firm transportation is deemed permitted by the present or future public convenience and necessity.

Transwestern's position is inconsistent with the express terms of the regulation it cites. Section 284.10(d)(1) provides only that "the pipeline may *file* under § 157.18

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[20] 41 FERC at pp. 61,448-49 (1987).

[21] Request for rehearing at 23-25.

[22] 18 C.F.R. § 157.18 (1987).

of this chapter to abandon sales service to the extent of the conversion." [Emphasis added]. The right to file for abandonment does not connote advance authorization. Nor is the statement in section 284.10(d)(2), that a customer's notice of intent to exercise an option to convert to transportation constitutes consent to abandonment, tantamount to advance approval by the Commission of the proposed abandonment. The future gas supply charge guidelines likewise do not provide for advance authorization of a pipeline's abandonment of its customers' CD entitlements in excess of their new sales nomination levels. Transwestern itself recognizes the need to obtain the Commission's prior approval for abandonment. As it states:

> Only by Commission grant of approval of Transwestern's application for permission to abandon firm sales above nominated levels could Transwestern permanently cease providing firm sales service. It was precisely for that reason that Transwestern filed its request for permission to abandon in Docket No. CP88-99-000.[23]

Moreover, Transwestern's argument that section 284.10(d) obviates the need for Commission review of the abandonment aspect of its GIC ignores the purpose of these regulations. The function of the regulations at section 284.10 is to increase buyer access to competitively priced sources of gas by broadening customer purchasing options through the availability of transportation service. While the future gas supply charge guidelines have as an overall goal increasing customer choice as to the source of gas, the immediate purpose of the guidelines is to encourage, through tangible economic incentives, realistic assessments of a customer's sales supply requirements *from the pipeline*. Thus, the CD conversion regulations relate to the sourcing of gas requirements from suppliers other than the pipeline transporting those requirements, whereas the future gas supply guidelines

[23] Request for rehearing at 30.

focus on the recovery of costs by the pipeline of maintaining access to gas which it will continue to sell for its customers.[24] We conclude that the regulations at section 284.10, whether considered independently or in conjunction with the Commission's prior approval in Transwestern's open access settlement of its standby service, do not constitute approval for the service contemplated in Transwestern's GIC.

2. Need for integrated review of Transwestern's GIC proposal and appropriate decisional standards

Clearly, Transwestern's proposal to abandon its service obligation with respect to its customers' CD entitlements in excess of their new nominations requires an amendment to its certificate under section 7. At issue is whether the remaining portion of its GIC proposal should be included in that analysis or be considered instead under the procedures and standards of section 4.

As Transwestern observes,[25] the appropriate decisional standards for reviewing a change in service depend upon the nature and extent of the contemplated change. While changes in the terms of service of a limited or minor nature may be considered under section 4, substantial changes in service must be reviewed and approved under section 7 before they can be put into effect. There is no precise rule that specifies when a change in the terms of service can be effected merely by a tariff change under section 4, or requires a certificate amendment under sec-

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[24] The distinction is one of substance, not form. For example, the future gas supply guidelines propose as their central feature, a monthly charge for maintaining gas *sales* inventory. Without doubt, this charge will be an important consideration in a customer's decision as to the amount of a pipeline's sales capacity to which it will commit. This charge is different from the reservation fee provided for in sections 284.10(c)(4) and 284.8(d), which relates to the reservation of *transportation* capacity.

[25] Citing *Reynolds Metals Co. v. FPC*, 534 F.2d 379 (D.C. Cir. 1976).

tion 7. In most instances the correct procedure under the statute will be clear, but in others, such as here, whether the change requires an application under section 7 may not be clear and require the exercise of judgment. Here, we concluded that Transwestern's implementation of the GIC and its concurrent abandonment of its customers' CD entitlements was a substantial change requiring scrutiny under section 7. The Commission reached this conclusion because in a close case the public interest purposes of the statute are best served by requiring Commission scrutiny under section 7 prior to the change taking effect.[26]

Transwestern argues that "implementation of the tariff sheets [containing the GIC] by placing them into effect . . . would in no way result in any abandonment of any certificated services."[27] It attempts to separate conceptually its concurrent abandonment application from its GIC filing, arguing that the GIC is merely a charging mechanism for a service that will continue. We agree that termination of Transwestern's firm sales obligation will technically arise as a result of Commission action on the application in Docket No. CP88-99-100 rather than in its separately docketed GIC filing. However, we fail to appreciate how Transwestern's filing of two separate applications attenuates the functional relationship between what are in reality two complementary aspects of its GIC proposal. As Transwestern itself notes, "An obvious consequence of a customer's nomination decision is loss of entitlement to higher firm sales volumes."[28] Further, in Section VI of its application in Docket No. CP88-99-000, Transwestern states:

> A necessary adjunct to the CDQ customers' right to freely nominate their level of CDQ is the attendant

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[26] *See Natural Gas Pipeline of America*, 41 FERC ¶ 61,358 (1987).

[27] Request for rehearing at 7.

[28] Cover letter accompanying Transwestern's December 1, 1987, at 16.

right of Transwestern to permanently abandon the level of CDQ not nominated under the applicable CDQ Rate Schedule.

The various aspects of Transwestern's GIC are an interrelated package of benefits and constraints that are intended to operate in tandem to produce an efficient and competitive sales function for Transwestern. In return for paying a known and firm monthly charge to reserve Transwestern's sales capacity and accepting a lower limit on its right to demand service, a Transwestern customer necessarily obtains a right to nominate the level of sales service it is willing to pay for. Because the various aspects of Transwestern's overall proposal are so closely and functionally related, sound regulatory policy requires that it be evaluated holistically under the same decisional standards. The segmented approach advanced by Transwestern, under which the Commission would carve out those aspects of its GIC proposal not related to the abandonment of sales service entitlements for separate consideration under section 4, would thwart the Commission's ability to review its proposal in a comprehensive and effective manner. Congress' intent is for the Commission to administer the provisions of the Natural Gas Act as a whole to protect the public interest.[29] After careful review, we have determined that the various aspects of Transwestern's GIC proposal, when taken together—as they necessarily must be—constitute a significant change in service requiring consideration under section 7. Only in this manner can the public interest be protected; conversely, the piecemeal approach requested by Transwestern would serve to undermine and frustrate our congressionally mandated oversight role.

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[29] *See Atlantic Rfg. Co. v. Pub. Serv. Comm'n*, 360 U.S. 378 (1959); and *FPC v. Louisiana Power & Light Co.*, 406 U.S. 621 (1972).

3. Other matters

Finally, Transwestern argues that in requiring review under section 7, the potential exists that it will be denied an opportunity to recover the cost of the firm standby sales service it claims it is now providing for a period in excess of the five-month maximum suspension period allowed under section 4.

First, by implementing the GIC, Transwestern would abandon rather than continue the existing standby service. Moreover, as previously discussed, Transwestern's cost of service is fully recovered without the need for a standby charge the Commission previously sought to impose.[30] Finally, under section 4, the Commission may suspend the effectiveness of a proposed change in service for up to five months. Had the Commission proceeded under section 4 and suspended the GIC for the maximum period, Transwestern could not have begun to charge under its GIC until June 1, 1988. Thus, even if we were to accept Transwestern's arguments, there is no current deprival of due process.[31]

Nor is our action tantamount to a retroactive conditioning of Transwestern's certificate. Transwestern itself has proposed a change in its certificate obligations which we have found must be reviewed under section 7. Thus, in requiring a certificate amendment for the GIC service, the Commission has not deprived Transwestern of its right to charge for an existing service, retroactively conditioned its existing certificate, or in any other way deprived it of its constitutional right to due process.

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[30] *See* discussion at n.n. 10 and 11, *supra*.

[31] Transwestern can make a rate filing under section 4 seeking recovery of any take-or-pay costs it has incurred prior to the time action is taken under section 7.

For the above reasons, Transwestern's request for rehearing will be denied. Arguments raised by Transwestern not specifically addressed are found to be without merit.

The Commission orders:

The request for rehearing filed by Transwestern Pipeline Company is denied.

FEDERAL ENERGY REGULATORY COMMISSION

Docket Nos. CP88-99-000, CP88-100-000,
and CP88-143-000

TRANSWESTERN PIPELINE COMPANY

ORDER ISSUING CERTIFICATES OF PUBLIC CONVENIENCE AND NECESSITY AND PREGRANTING ABANDONMENT AUTHORITY

(Issued May 11, 1988)

Before Commissioners: Martha O. Hesse, Chairman; Anthony G. Sousa, Charles A. Stalon, and Charles A. Trabandt.

Background

On December 1, 1987, Transwestern Pipeline Company (Transwestern) submitted three interrelated filings. In its filing, initially docketed as Docket No. RP88-35-000 and subsequently redocketed as Docket No. CP88-143-000, Transwestern proposed to establish a Gas Supply Inventory Charge (GIC), purportedly in compliance with the guidelines established in Order No. 500.[1] In Docket No. CP88-99-000, Transwestern filed an abbreviated application for certificate authority to implement an off-system and on-system interruptible sales service and for pregranted authority to abandon this service. In Docket No. CP88-100-000, Transwestern requested pregranted approval for the abandonment of its existing firm sales service to the extent such sales exceeded customer nominations under the GIC proposal.

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[1] *FERC Statutes and Regulations* ¶ 30,761 (1987).

On December 7, 1987, the Commission issued a notice in Docket No. CP88-143-000 concerning Transwestern's proposed tariff sheets.[2] Twenty-one timely, unopposed motions to intervene were filed, all of which were granted by a Commission order issued on December 31, 1987.[3] Untimely motions to intervene under this docket were filed by El Paso Natural Gas Company, Texas Eastern Transmission Corporation (TETCO), Citizens Energy Corporation *et al.* (Citizens), Southern California Utility Power Pool *et al.*, and Southern California Edison Company (Cal Edison).

On December 8, 1987, the Commission issued notices of Transwestern's applications in Docket Nos. CP88-99-000 and CP88-100-000.[4] In Docket No. CP88-99-000, seventeen timely notices or motions to intervene were filed.[5] Untimely notices or motions to intervene were filed by TETCO, Kansas Corporation Commission (KCC) and Hadson Gas Systems, Inc. (Hadson). Protests were filed by Southern California Gas Company (SoCal), California Public Utilities Commission (CPUC), Natural Gas Clearinghouse, Inc. (clearing house) and Kansas Power and Light Company (KP & L). ANR Pipeline Company (ANR) and Colorado Interstate Gas Company (CIG) filed a joint request to dismiss the application or hold it in abeyance. SoCal and CPUC filed separate requests for hearing. In Docket No. CP88-100-000, twelve timely notices or motions to intervene were filed.[6] Untimely motions to intervene were filed by TETCO, KCC, Cal Edison

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[2] 52 Fed. Reg. 47,046 (December 11, 1987).

[3] 41 FERC ¶ 61,371 (1987). The order incorrectly states that the interruptible sales proposal was docketed as Docket No. CP88-100-000 and that the application to abandon sales entitlements in excess of the GIC nominations was docketed as Docket No. CP88-99-000.

[4] 52 Fed. Reg. 47,449 (December 14, 1987).

[5] These motions are listed in Appendix A.

[6] *See* Appendix B.

and Kern River Gas Transmission Company. SoCal and CPUC filed separate requests for hearing and CPUC filed a protest. Timely notices and motions to intervene are granted by operation of Rule 214 of the Commission's Rules of Practice and Procedure.[7]

In light of the early stage of this proceeding and the absence of prejudice to any party, we will grant all of the late-filed motions to intervene in Docket Nos. CP88-99-000, CP88-100-000 and CP88-143-000. However, as discussed below, the requests for hearing will be denied. The concerns raised in the protests are addressed below and in the conditions attached to the certificates granted below.

In its December 31, 1987 order, the Commission found that adoption of the GIC would result in fundamental changes in the service relationship between Transwestern and its customers that required amendment of Transwestern's existing sales certificate under section 7. The GIC filing under section 4 was redocketed and the tariff sheets containing the GIC were held for consideration as *pro forma* sheets in the newly instituted section 7 proceeding. In its December 31, 1987 order, the Commission consolidated the three filings noted above and directed the Commission's staff to convene a technical conference to examine the extent of competition in Transwestern's markets and other issues raised by the three filings.[8]

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[7] 18 C.F.R. § 385.214 (1987).

[8] On January 29, 1988, Transwestern filed a request for rehearing of the Commission's December 31, 1987 order in which it disputed the Commission's finding that the GIC would fundamentally alter its service relationship with its customers. In an order, issued March 25, 1988, the Commission rejected Transwestern's contentions and affirmed its decision to consider the GIC in Docket No. CP88-143-000 under the procedures and standards of section 7. 42 FERC ¶ 61,370 (1988).

Technical conferences were held on January 22, 1988 and on February 25, 1988, at which the parties discussed a number of factual and policy issues. The primary focus of concern was the GIC filing and whether it was cost-based, as asserted by Transwestern, or if not cost-based, whether competition in the affected market was sufficient to keep the GIC in a just and reasonable range. After the conferences, interested parties filed statements of position addressing the issue of whether a hearing was required to adequately consider the aspects of Transwestern's proposal which affected them.[9] Several parties submitted replies to the statements of other parties.

Discussion

On the basis of the record developed to date, the Commission concludes that the contested issues involve matters of policy rather than fact. Courts have clearly established that no evidentiary hearing is required where there is no dispute of material facts. Although SoCal, CPUC and other parties draw different inferences and conclusions from the evidentiary facts than does Transwestern, particularly as to whether the GIC mechanism is cost or market-based, there is little disagreement as to the facts underlying their disparate positions.

Gas Inventory Charge

1. Transwestern's Proposed Service

The GIC would be applicable to Transwestern's CDQ sales customers. At present, Transwestern has two CDQ customers, SoCal and Williams Natural Gas Company (Williams). However, Williams, pursuant to the terms of its existing CDQ sales contract, gave notice on February 1, 1988, that it would terminate the contract effective February 1, 1989, and in its statement of position it stated that it would nominate zero volumes for the GIC.

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[9] Parties filing statements of position are listed in Appendix C.

Thus, only SoCal would be directly affected by the GIC, although Transwestern serves a number of small full requirements sales customers that would be indirectly affected in that these customers' rates would be based on the level of service nominated by SoCal.

Under the GIC, as proposed, Transwestern would post the price levels for its commodity charges and associated GICs 30 days prior to the date they would become effective. SoCal would then nominate its desired level of sales service, up to its current certificated contract demand (CD) quantity, within a 15-day nomination period. As discussed more fully below, Transwestern would abandon its service obligation to the extent SoCal's GIC nomination was less than its existing CD quantity.

Nominations for the first 367,500 Dth per day of gas are described as the "base purchase volume." [10] These nominations would be effective for an entire year, and SoCal would be required to nominate the same level of service for each day of the year. Nominations in excess of the base purchase volume are described as "incremental" purchase volumes, and SoCal would be entitled to nominate its desired level of service on a quarterly basis. However, the same level of service would be applicable for each day in the quarterly nomination period.

The first 157,500 Dth per day that SoCal would nominate is described as a "forward supply service." According to Transwestern, this quantity consists of casinghead gas, drainage gas, and gas subject to the minimum take levels in Transwestern's contracts.[11] SoCal would be re-

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[10] The base purchase volume (roughly equivalent to 350,000 Mcf per day at 1,050 Btu per Mcf) represents the approximate deliverability of supply committed to Transwestern which it projects will be available for sale during calendar 1988.

[11] Transwestern has supplied data showing casinghead and plant gas volumes of 64,000 Dth per day, with an average cost on a unit of purchase basis of $2.20 per Dth. Because of state proration-

quired to take 100 percent of its nominations within the forward supply service quantity, and would be assessed a GIC of a percentage of the gas cost component for shortfalls below its nominated level. Quantities above 157,500 Dth per day are referred to as an "option service." The option service would not be available unless SoCal first agreed to take the full quantity contained in the forward supply service. As proposed by Transwestern, the tariff language is unclear as to whether SoCal could nominate a level of service below the forward supply ceiling of 157,500 Dth per day or is limited to choosing between nominating zero or the full ceiling quantity. In addition to the 100 percent take requirement with respect to forward supply volumes, the GIC would be assessed under the option service whenever SoCal's takes fall below 85 percent of its daily nominations. No make-up period is provided.

During the period in which the GIC is in effect, Transwestern has proposed to suspend the operation of its PGA mechanism. Any balance in its Account No. 191 (Unrecovered Purchase Gas Costs) attributable to the period prior to implementation of the GIC is proposed to be directly billed or refunded to its customers. Transwestern has reserved the right to reinstate its PGA on 30 days' notice in the event it terminates the GIC.

Transwestern states that the GIC reflects its estimate of its cost to maintain an inventory of gas to meet customer nominations, including amounts paid to a seller as an inventory charge and the cost-of-service effects of traditional take-or-pay payments.[12] Transwestern has in-

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ing laws, these are likely to be the first volumes purchased by Transwestern. The first 50,000 Dth per day under the GIC has an average cost on a unit purchase basis of $7.76 per Dth.

[12] Transwestern application at p. 20. In its Stateemnt of Position, Transwestern asserts that in calculating the GIC, it analyzed the cost of connected supplies, the take-or-pay levels of such contracts, and the costs incurred to buy out take-or-pay exposure under exist-

cluded in its filing a *pro forma* Sheet No. 5E intended to illustrate the anticipated level of the GIC based on various nomination and purchase assumptions for the option service. The data in Sheet No. 5E are stated to be based on information available to Transwestern at the time of its filing. The GIC ranges from $.42 per Dth for purchase shortfalls for nominations under the options service of 315,000 Dth per day or less to $.33 per Dth for certain shortfalls below nomination quantities greater than 315,000 Dth per day.

2. Position of the parties

Transwestern's position is that its GIC proposal is both cost-based and subject to competitive market forces. SoCal argues, in contrast, that the price/quantity commitments under the GIC are neither cost-based nor market-based. SoCal notes that Transwestern has structured these commitments to require purchases of its most expensive gas first, with successively less expensive supplies available as purchase volumes increase. It contends that this sequencing method differs from Transwestern's actual purchasing practices and would permit Transwestern to overrecover costs and earn an excessive return on its merchant function.

SoCal also objects to the provision in the GIC under which it would be required to nominate either zero volumes or the entire quantity under the forward supply service as contrary to the purpose of Order No. 500. It regards the forward supply service as a noncompetitive market structuring mechanism which deprives it of choice and flexibility in meeting its supply needs. SoCal likewise complains that the supply sequencing method proposed in the GIC is anticompetitive in that its resale customers cannot sustain the prices derived under this method.

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ing contracts, as well as the projected costs for reserving supply under new contracts for firm sales. *Id.* at 38.

SoCal requests the Commission to modify Transwestern's proposal in certain respects to remedy the purported deficiencies discussed above. First, SoCal requests that the GIC not be assessed unless its purchases drop below Transwestern's system average take-or-pay level of 68 percent. It argues that the higher thresholds proposed by Transwestern would permit Transwestern to collect revenues under the GIC even though it incurred no take-or-pay costs.

SoCal opposes Transwestern's proposal to reinstitute its PGA on 30 days' notice on the grounds that it will insulate Transwestern from the risk of undercollection of its gas supply costs. It asserts that the reinstitution option will provide Transwestern with the benefits of both the GIC and PGA cost recovery mechanisms without the attendant burdens of either. SoCal requests the Commission to postpone reinstitution of Transwestern's PGA until after a final Commission order has been issued under either section 4 or section 7. SoCal also objects to Transwestern's proposal to directly bill any balances remaining in its Account No. 191. It complains that it would be required to absorb more than 85 percent of any unrecovered balances under Transwestern's proposal. SoCal requests that the unrecovered balances be collected instead solely through the commodity charge under the GIC.

SoCal complains that although it would be required to purchase supplies from Transwestern under the GIC, Transwestern is not under any corresponding obligation to warrant the security of the supplies which SoCal nominates. SoCal requests the Commission to require Transwestern to replace exculpatory language under the GIC with an affirmative statement of its supply obligations excused only by reason of *force majeure*. Finally, SoCal requests the Commission to require Transwestern to remove the minimum take provision in the forward supply service and to restructure the price/quantity commitments to reflect a least cost purchasing strategy.

CPUC also disputes Transwestern's position that competition can be totally relied upon to keep Transwestern's prices just and reasonable and that the GIC reflects Transwestern's actual cost of service. CPUC states that although it shares the Commission's objective to move toward greater reliance on competition in the regulation of natural gas companies, it does not consider Transwestern's GIC, as proposed, to further this goal. It contends that most of SoCal's customers are captive and unable to switch to alternate supplies. CPUC further asserts that the competitive benefit of access by SoCal to transportation capacity on Transwestern's system may be undermined by a lack of long-term supply availability in Transwestern's producing area. CPUC acknowledges that SoCal has had recent experience in sourcing its supply requirements, but asserts that Transwestern's level of expertise in this area is much greater. CPUC is also concerned about the status of any long-term contracts SoCal might enter into in the event Transwestern sought to reinstitute its PGA or abandon its open access certificate. CPUC complains that the quality of service which would be available under the GIC will be lower than that now enjoyed by SoCal under its CD entitlement from Transwestern. It is also concerned that in the event SoCal nominated zero quantities under the GIC, the 15-day GIC notice period would give SoCal insufficient time to arrange for alternate supplies.

CPUC disputes certain assumptions underlying Transwestern's position that the GIC is cost based. It contends that Transwestern can obtain buyout relief from its take-or-pay contracts at a cost of less than the 25 cents per dollar claimed by Transwestern. CPUC also considers the daily GIC thresholds proposed by Transwestern to be too tightly constructed in view of Transwestern's annual make-up privileges and general lower level of purchase responsibility under its take-or-pay contracts. Finally, CPUC is concerned that the price/quantity commitments included in Transwestern's filing are illustrative only and

will not necessarily reflect Transwestern's actual GIC rates.

CPUC shares SoCal's concerns that Transwestern's proposed supply sequencing method fails to reflect Transwestern's least cost purchasing pattern and ongoing program to reform its problem contracts. Since the price/quantity commitments will be in effect for the entire year, CPUC argues that Transwestern will benefit from any reformations completed during that period. As a constraint on Transwestern's GIC pricing formula, CPUC proposes that the Commission provide a procedure for protests and refunds of any amounts later determined to be excessive under the GIC.

CPUC reiterates SoCal's objections to the all-or-none requirement in the forward supply service and Transwestern's proposed direct billing of its Account No. 191 balance. Finally, CPUC proposes that in the event the Commission approves direct billing, it should cap customers' respective shares at 50 per cent of the total Account No. 191 balance. A number of additional parties shared these and other concerns in their statements of position. The Commission has considered their views in its analysis below.

3. Discussion

One of the principal goals of the Natural Gas Act is to assure consumers adequate long term supplies of natural gas at reasonable prices. Through the Natural Gas Policy Act, Congress has also sought to establish competitive markets for natural gas at the wellhead, and charged the Commission with its implementation. Although we have traditionally applied cost-of-service principles to most of our rate determinations, the Commission has considerable flexibility in selecting the methodology it will use to determine a just and reasonable rate.[13] Where

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[13] *See, e.g., Permian Basin Area Rate Cases*, 390 U.S. 747, 790 (1968).

competitive conditions exist, the Commission has flexibility to oversee markets entrusted to it with a lightened regulatory hand. Clearly identified non-cost factors such as competition or lack of market power may warrant a departure from the traditional rate review process where the substitute ratemaking methodology ensures that resulting rate levels are justified by those factors.[14] Thus, in *Farmers Union Central Exchange*, the court of appeals recognized that light-handed regulation and a reliance on market forces can be justified where the Commission can "demonstrate that market forces can be relied upon to keep prices at a [just and] reasonable level." [15] Thus, in order to authorize the flexible pricing embodied in Transwestern's GIC, we must (1) find that market-oriented pricing would promote the statutory objectives of the Natural Gas Act; (2) find substantial evidence that competition in the relevant markets will operate as a meaningful constraint on the exercise of market power on the part of Transwestern and (3) establish that the market-oriented pricing mechanism, subject to a cost based cap or other constraint, will produce rates that invariably fall within a zone of reasonableness so that market forces will not be the exclusive means through which to arrive at just and reasonable rates.

Based on the evidence presented in Transwestern's filings and elicited from Transwestern and other parties subsequent to the technical conference, the Commission concludes that Transwestern's proposal satisfies the public convenience and necessity standards of the Natural

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[14] *Natural Gas Pipeline Company of America*, 41 FERC ¶ 61,358 (1987), *citing Farmers Union Cent. Exchange, Inc. v. FERC*, 734 F.2d 1486, 1501-1503, 1509-1510 (D.C. Cir. 1984); and *FPC v. Texaco Inc.*, 417 U.S. 380 (1974). Additional precedents concerning the role of competition in shaping the Commission's ratemaking function are summarized in *Pacific Gas and Electric Company*, 38 FERC ¶ 61,030 (1987); and *Tenneco Oil Company*, 26 FERC ¶ 61,030 (1984).

[15] *Farmers Union Cent. Exchange v. FERC*, *supra* at 1510.

Gas Act, with certain conditions. The Commission further finds that Transwestern lacks market power in the southern California market in which Transwestern operates and that SoCal has alternative sources of supply available to it sufficient to exert substantial downward pressure on the prices which would be posted by Transwestern in its GIC.

a. The relevant market.

In its December 31, 1987 order, the Commission noted that Transwestern had provided a substantial amount of information to establish the competitiveness of its markets, at least with respect to its largest customers.[16] The Commission has considerable flexibility in selecting the methodology it will use to determine a just and reasonable rate.

Review of the record here confirms our prior assessment that the market in which the GIC will operate is sufficiently competitive so that the rates charged will be just and reasonable. We discuss below the salient competitive features of the southern California market which lead us to this conclusion.

First, Transwestern has presented evidence, not disputed by SoCal, that SoCal has access to substantial sales and transportation capacity on a number of pipeline systems apart from Transwestern. SoCal's current suppliers include:

Transwestern	750 MMcf/day [17]
El Paso	1,750 MMcf/day [18]

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[16] 41 FERC at p. 62,006 (1987).

[17] The volumes listed for Transwestern and El Paso are contract demand levels.

[18] El Paso Natural Gas Company. El Paso also currently provides transportation pursuant to section 311.

PITCO	240 MMcf/day [19]
POPCO	26 MMcf/day [20]
PIOC	55 MMcf/day [21]
PGT (through PG&E)	177 MMcf/day [22]
Intrastate and outer continental shelf	220 MMcf/day [23]

In addition, Transwestern states that SoCal has access to other Canadian gas supplies through interconnections between Northern Border Pipeline, Northern Natural Gas Company and Transwestern. SoCal has extensive storage facilities with aggregate capacity of 117 Bcf and a record withdrawal rate of 2.568 Bcf per day. Transwestern itself does not have any storage facilities. During 1987, purchases from Transwestern accounted for only about 10 percent of SoCal's total purchases.

Transwestern further argues without dispute from SoCal that SoCal has experience in negotiating long-term

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[19] Pacific Interstate Transmission Company (PITCO) supplies Canadian gas to SoCal. The contract is for 240 MMcf per day with a 60 percent minimum bill. The volumes are delivered to the southern California border by El Paso. As such, some of these volumes may overlap with those shown for El Paso because the gas is delivered through El Paso's capacity to SoCal.

[20] Transwestern states that Pacific Offshore Pipeline Company (POPCO), an affiliate of SoCal, averaged sales of 26 MMcf per day to SoCal in 1987. POPCO's 1987 FERC Form 2 shows annual sales to SoCal of 9,205,704 Mcf or 25 MMcf/day.

[21] Transwestern states that Pacific Interstate Oil Company (PIOC), also a SoCal affiliate, averaged sales of 55 MMcf per day to SoCal in 1987. PIOC's 1987 FERC Form 2 shows annual sales to SoCal of 20,738,654 Mcf or 57 MMcf/day.

[22] Canadian supply is also sold to SoCal through an interutility exchange with Pacific Gas and Electric Company (PG&E). In 1987, an average of 177 MMcf per day was purchased by SoCal through this route.

[23] This is primarily associated gas. Purchases in 1987 averaged 220 MMcf per day. This total does not include any gas purchased from POPCO.

and firm contracts. SoCal has several producing affiliates, such as Pacific Lighting Oil and Gas Company, that could assist SoCal in securing long term gas supplies. Additionally, SoCal is affiliated with several interstate pipelines, including PITCO and POPCO. By order,[24] issued March 1, 1988, the Commission approved Transwestern's application for a blanket transportation certificate, which has since been accepted by Transwestern. Thus, SoCal has direct access to long term supplies located in Transwestern's supply area.

SoCal has not argued that it would be unable to contract for alternate supplies if the GIC is implemented. It contends, rather, that implementation of the GIC would render the market for long-term supplies in southern California not workably competitive, at least in the short run. Under California regulations, SoCal must divide its market into core customers and non-core customers. The core customers are generally residential and small commercial users. Under California regulations, these customers will be served primarily using long term firm gas supplies. The non-core customers will be served primarily with short term supplies. The 1987 California Gas Report [25] estimated that in a cold temperature year, the core requirements would be approximately 1,300 MMcf per day.[26] The California Gas Report shows total available gas supplies to SoCal of 4,800 MMcf per day. Included in this amount are 1,000 MMcf per day of short-term supplies and 500 Mcf per day of transportation gas.

At present, based on data furnished by Transwestern and not disputed by SoCal, Transwestern's gas supplies

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[24] 42 FERC ¶ 62,187 (1988).

[25] This report is published by the state of California and is prepared using data submitted by the gas and electric utilities located in that state.

[26] Total requirements (including non-core customers and others) in a cold temperature year are estimated at 2,900 MMcf per day, including 500 MMcf per day of transportation gas.

at peak capacity in 1987 constituted approximately 23 percent of SoCal's available supplies. As noted, SoCal, unlike Transwestern, has extensive storage facilities which provide it with additional flexibility in meeting its peak needs. Thus the data indicate that even without purchases from Transwestern, SoCal has sufficient supplies available to it to fulfill its service requirements.

In addition, data indicate that Transwestern lacks significant market power in the supply areas in which it purchases gas. Transwestern's supplies are primarily located in eastern New Mexico (the Permian Basin), Texas Railroad District Nos. 8 and 10, and in Oklahoma.[27] In 1986, only 15 percent of the reserves in eastern New Mexico (the Permian Basin) were committed to Transwestern; in Texas Railroad District No. 8, 10.5 percent of the reserves were committed to Transwestern and in Texas Railroad District No. 10, 4.6 percent of the reserves were committed to Transwestern; and in Oklahoma only 2.3 percent of the total was committed to Transwestern.[28] The total reserves committed to Transwestern in 1986 averaged only 6.5 percent of the total reserves available in these areas. Moreover, the available data shows that there have been and should continue to be ample uncommitted reserves available for SoCal to purchase in Transwestern's supply area. The amount of uncommitted reserves in Transwestern's supply area in 1984 were at least 1.4 Tcf and potentially of 7 Tcf.[29] Since then interstate pipelines have been reducing reserves under contract in that area, from 18.57 Tcf in 1984 to 16.2 Tcf in 1986, while total reserves have re-

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[27] *See* Appendix D for a more precise breakdown.

[28] *See* Appendix E for detailed breakdown of reserves and production allocated to Transwestern in its supply area.

[29] See Appendix F. All figures shown are from EIA data or FERC Form 15.

mained unchanged.[30] Although 1987 data will not be available until September 1988, there is nothing to lead the Commission to believe that these trends have changed. From 1978 through 1984 (the last year data was available) there was consistently at least 1 Tcf of uncommitted gas in the areas in which Transwestern purchases its supplies,[31] and this is consistent with the persistent surplus that has existed since the early 1980's and currently exists nationally.[32]

CPUC argues that SoCal would not be able to contract with producers for the same quality of service as Transwestern provides. The basis for this claim, CPUC states, is that producers are reluctant to enter into new long-term contracts but Transwestern still has long-term supplies under contract. However, the CPUC ignores the fact that Transwestern's long-term contracts are the ones that, for the most part, are priced above the current market, and the CPUC and SoCal have argued here that SoCal should not have to pay the full price of those contracts. If those contracts are as highly valued as the CPUC claims, then SoCal should be expected to pay their price. Transwestern's market-priced contracts generally include market-out clauses[33] under which the prices can be revised or the contracts can be terminated and any new contracts that Transwestern would enter into would have similar provisions. Therefore, Transwestern is not in a better position to acquire firm, long-term supplies than is SoCal. Moreover, the relevant question is not

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[30] *Id.*

[31] *Id.*

[32] *Compare* EIA, Natural Gas Monthly, Table 6 (Jan. 1988) (Appendix G) *with* Appendix F.

[33] Transwestern's long-term, below market-priced contracts would be subject to the good-faith negotiation rule of section 270.201 of the regulations and therefore, are subject to renegotiation of the price or termination.

whether the type of contracts SoCal could enter into with alternative suppliers would be identical, but whether they would be a reasonable substitute to service from Transwestern. While there may be regulatory differences between sales by producers and sales by pipelines that result in differences in contracts or service, Congress determined when it enacted the NGPA that purchases from producers are a reasonable substitute for purchases from regulated pipelines.[34]

In short, the Commission finds no basis for the claim that SoCal will be unable to acquire alternative supplies in Transwestern's supply area either in the long term or the short-term. In view of the alternate supplies available to SoCal to meet its requirements from competing sources, the Commission concludes that SoCal could arrange to totally replace Transwestern as a merchant supplier. This conclusion is supported by the relative sophistication of SoCal in meeting its requirements from competing sources.[35] If this conclusion proves to be incorrect, the Commission has adequate remedial power to ameliorate any problems which develop.

b. Constraints on Transwestern's charges.

The Commission finds that because SoCal has alternative sources of supply available to it, these alternatives will act as a restraint on Transwestern's prices to insure that they remain in a just and reasonable range. As discussed above, SoCal can purchase gas from other sources at just and reasonable rates. Either SoCal can purchase supplies from other pipeline sources at regulated

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[34] Of course, the CPUC will be able to scrutinize the prudence of the choices SoCal makes as to its suppliers in determining the rates regulated by the CPUC. *Kentucky West Virginia Gas v. Pa. Public Utility Comm'n*, 837 F.2d 600 (3rd Cir. 1988).

[35] The variety of sources from which SoCal has been obtaining its gas supplies belies any claim that SoCal is an unsophisticated gas buyer.

rates or, more significantly, it can purchase directly from producers at prices that Congress has deemed to be just and reasonable in NGPA section 601(b), plus the cost of transportation at Commission-regulated rates.

Thus, the availability of these alternative supplies, at just and reasonable rates, will serve as a check on Transwestern's gas inventory charge because Transwestern must keep its charge at or below these alternatives in order to retain SoCal as a customer.[36] Because SoCal is Transwestern's only remaining large customer, Transwestern must consider SoCal's supply alternatives in posting its price/quantity commitments. Further, because SoCal is not a captive customer, Transwestern has the incentive to keep its gas costs as low as possible so as to retain SoCal's business. The record indicates that Transwestern has already taken steps to reduce its gas costs through purchases of market responsive gas and renegotiation of its problem contracts.

Inasmuch as this new service is essentially a two party transaction, between Transwestern and SoCal, there is every reason to expect that they can and will negotiate terms and prices that are mutually acceptable. Otherwise, SoCal can purchase its gas supply needs from other sources, using Transwestern for transportation only. The sophistication of SoCal as a buyer in the gas market, Transwestern's lack of market power either as a seller or buyer of gas, and the availability of alternative supplies at just and reasonable prices all justify the use of a lighter regulatory hand in this case. Thus, many of the conditions urged by SoCal or the CPUC are unnecessary for this certificate.[37]

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[36] *See Baltimore Gas and Electric Co.*, 40 FERC ¶ 61,170 (1987).

[37] San Diego Gas and Electric Co., a customer of SoCal, argued that it should be permitted direct access to firm interstate capacity on Transwestern's system. SoCal and the CPUC argue that this is beyond the scope of this GIC proceeding and is best addressed elsewhere, specifically in state proceedings. The Commission agrees that the issue is beyond the scope of this proceeding.

4. Conditions

In order to insure that the GIC mechanism functions as intended, the Commission will condition its approval in a number of ways.

a. Nomination time frame.

The GIC is being approved because the Commission has concluded that the availability to SoCal of alternative supplies will keep Transwestern's rates within a just and reasonable range. In order to strengthen SoCal's ability to arrange alternate sources and, therefore, competitive market conditions, we will extend the proposed notice period from 15 to 45 days for the annual volume commitments. For the quarterly commitments, SoCal's nominations will be extended to 30 days.[38]

b. Unrecovered purchased gas costs.

SoCal opposes Transwestern's proposal to directly bill undercollections in its Account No. 191 to account for prior period adjustments and refunds incurred prior to July 1, 1988. It argues that direct billing is contrary to Commission policy and inconsistent with the Commission's responsibilities under section 4 to exercise continuing regulatory oversight with regard to costs and charges flowed through to Transwestern's customers. SoCal asserts that any undercollections may be recovered through a commodity charge. SoCal's position is rejected. Since it may nominate zero volumes under the GIC, recovery of undercollections as a commodity charge is not feasible. As Transwestern will terminate its PGA when the GIC is instituted, the most appropriate method of recovery is

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[38] For the first year the GIC is in effect, SoCal will have an additional 45 days, inasmuch as Transwestern will have (as discussed below) 45 days to advise the Commission as to whether it will accept the GIC certificate as conditioned. Once Transwestern accepts the certificate and posts its rates, SoCal will have 45 days after that date to make its annual nominations.

direct billing. In the event SoCal's nominations under the GIC are zero, Transwestern may bill 85.7 percent of undercollections to SoCal and the remainder to Williams.

The Commission will permit this procedure as a reasonable transitional mechanism. The amounts in the deferred account are amounts incurred by Transwestern to sell gas to its customers in the past; therefore, it is appropriate for these customers to be billed to clear the account upon termination of Transwestern's PGA.[39]

c. Maintenance of adequate supplies.

Since Transwestern is proposing to assess the GIC on all volumes which are taken by SoCal, it must warrant both the base and incremental volume commitments it has agreed to deliver. In line with this supply obligation, the Commission will require Transwestern to credit GIC revenues against future GIC costs if it fails to deliver gas in the future. However, our acceptance of this crediting requirement should not be construed as limiting other contractual remedies SoCal may have if Transwestern fails to deliver. In addition, Transwestern must remove any exculpatory language from its tariff regarding its failure to deliver.[40] This language should be replaced with language providing for an obligation to perform except by reason of *force majeure.*

d. Rates for IS and non-CDQ sales customers.

The Commission concludes that the WACOG for Transwestern's captive Rate Schedule SG and RW customers should be set at the lower of Transwestern's WACOG in its current PGA or the rate to be charged SoCal under the GIC. These small customers' gas costs should remain

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[39] If Transwestern's Account No. 191 reflects overcollections, Transwestern shall refund the amounts to its customers.

[40] *Cf. Texas Eastern Transmission Corporation,* 41 FERC ¶ 61,373, at p. 62,019 (1987).

in effect for at least the first year of the GIC. Although we are permitting Transwestern to file for revised rates for the second year the GIC is in effect, this should not be construed as an indicia of pregranted approval of any proposal it may file. Any subsequent proposal filed by Transwestern will be reviewed by the Commission and be either accepted, rejected or suspended, as appropriate.

The Commission further concludes that the floor price to be charged Transwestern's new interruptible off-system sales customers, as discussed below, should be set at the WACOG included in the rate to be charged to Transwestern's small Schedule SG and RW customers. This condition is necessary to ensure that Transwestern cannot segment its markets by charging these customers a higher price than other customers having broader purchasing options. This will remove the potential for undue discrimination in Transwestern's current proposal, which would provide preferential rates to interruptible off-system customers at the expense of firm on-system customers.

e. Reinstatement of Transwestern's PGA.

In its GIC proposal, Transwestern has reserved the right to reinstate its PGA on 30 days' notice. Under section 154.303(b) of the regulations,[41] a pipeline may recover changes in its purchased gas costs either by filing a request for a change in its rate level under section 154.63 of the regulations[42] or by complying with the election procedures in section 154.303(b). The election procedures provide for an initial election commencing on June 1, 1988 and on January 1 of each third year thereafter. Section 154.303(b)(6) of the regulations provides that a pipeline which has elected the non-PGA option for an election period may file revised tariff sheets

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[41] *FERC Statutes and Regulations* ¶ 30,778 (1987), to be codified at 18 C.F.R. § 154.303(b).

[42] 18 C.F.R. § 154.63 (1987).

implementing the PGA clause option for the next election period. This election must be made on or before December 1 of the year preceding the commencement of an election period.

Transwestern's proposal is inconsistent with these regulations, and our approval of the GIC proposal will be conditioned on the deletion therefrom of Transwestern's reserved right to reinstate its PGA on 30 days' notice. In order to reinstate its PGA, Transwestern must file under section 4 of the Natural Gas Act and in accordance with the procedures in section 154.303 of the regulations, and demonstrate that it is entitled to a waiver if it wants to reinstate its PGA at an earlier time than provided in those regulations. Further, because we have already determined that certificate authority must be obtained prior to the institution of service under the GIC, Transwestern must likewise obtain a certificate to abandon or revise the GIC in the future. Therefore, until the GIC is abandoned, it will remain an available service provided by Transwestern even if it reinstitutes its PGA.

f. Exit fee.

As noted, the proposal is being approved on the basis that competitive forces will act as a check on Transwestern's rates to keep them within a just and reasonable range. SoCal's ability to arrange for alternate supplies is an important assumption underlying the Commission's approval here.

Thus, if Transwestern posts rates that are unreasonable given current market conditions, it is rational to assume that SoCal will nominate zero purchases for the GIC. SoCal should know the full cost consequences of its nominations in advance. As such, Transwestern should not be able to impose an exit fee (or a surcharge on transportation rates) if SoCal chooses to nominate zero because Transwestern's rates are not competitive. Fur-

ther, Order No. 500 provides that the GIC is to be the sole mechanism for recovery of future take-or-pay costs. This guideline would be undermined if Transwestern were permitted to charge its customers for future take-or-pay costs through both the GIC and an exit fee. Thus, once the GIC takes effect, Transwestern cannot recover take-or-pay costs it might incur because of the level of SoCal's nominations apart from the GIC. Any take-or-pay costs that Transwestern has already incurred prior to acceptance of the GIC certificate can be recovered under the Commission's policies as set forth in Order No. 500.

GIC Abandonment Application

In Docket No. CP88-100-000, Transwestern has requested pregranted authority to abandon certain levels of presently certificated CDQs to the extent a CDQ customer does not nominate the full CDQ level under the GIC nominations procedure. The abandonment authorization would apply to both the initial nominations and those made in future years. Transwestern states that any CDQ reductions will be deemed to be converted to firm transportation under the FTS rate schedule. Transwestern proposes that the abandonment authorization would be effective with the effective date of the initial nominations under the GIC. Transwestern would file tariff sheets reflecting the revised service levels within 15 days of the effective date of any permanent abandonment. Transwestern asserts that the abandonment proposal is necessary: (1) to renegotiate its supply contracts to reflect market realities at the distribution end of its system; (2) to effectively manage its gas supplies; and (3) to avoid any unnecessary costs where conversion rights have been exercised.

No opposition to the abandonment proposal has been filed, and Transwestern's stated justifications for the proposal are persuasive. Abandonment authority is nec-

essary to implementation of the GIC. As indicated above, the Commission finds that the public interest will be served by approving that proposal as conditioned. Accordingly, we find, pursuant to section 7(b) of the NGA, that the present and future public convenience and necessity permit such abandonment.[43]

Interruptible Sales Program

1. Transwestern's Proposed Service

In Docket No. CP88-99-000, Transwestern seeks authorization to establish an Interruptible Sales Rate Schedule (IS-1) and requests blanket certificate authority to make interruptible sales of natural gas for resale to on-system and off-system interstate pipelines, Hinshaw pipelines, and local distribution companies (LDCs) pursuant to the provisions of that new rate schedule. Transwestern's CDQ customers would be able to purchase IS-1 gas in any amount that exceeds their certificated level as nominated under the GIC. Transwestern also requests blanket authority to effectuate deliveries of interruptible direct sales to on-system and off-system end users under terms and conditions similar to those contained in the IS-1 Rate Schedule.

All the interruptible sales will be made from Transwestern's available natural gas supplies which are surplus to the daily needs of Transwestern's existing firm sales customers. Transwestern also requests pregranted authority to abandon sales to any purchaser under Rate Schedule IS-1, or deliveries to any end user, at the end of the term of the underlying service agreement or sales contract between Transwestern and the IS purchaser.

Transwestern proposes to charge a negotiated rate within a specified range for the IS-1 sales service. The maximum rate would be equal to the 100 percent load factor rate for the CDQ-1 sales rate. However, if the GIC is in effect, the maximum rate would be the 100

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[43] See 15 U.S.C. § 717f(b).

percent load factor using the highest gas cost component set forth in the price/quantity commitment for the GIC. If the GIC is in effect, the minimum rate would be the actual incremental cost of purchased gas plus fuel, other variable costs, and GRI and ACA surcharges. Transwestern proposes to retain all revenues received from the IS-1 sales.

No new facilities are proposed for the IS-1 sales. IS-1 purchasers would be responsible for all arrangements and costs related to third-party transportation. Furthermore, interruption or curtailment of IS-1 sales would be implemented on the same basis as is applicable to interruptible transportation services, as set forth in section 22 of Transwestern's tariff.

Transwestern has suggested that to permit monitoring of the IS-1 sales, it would file reports similar to those contained in sections 284.106(a) and 284.106(c) of the Commission's regulations.[44] Under this procedure, Transwestern would file an initial report within 30 days of commencement of the sale detailing the purchaser, the sales rate, and the term of the sale. Actual volumes sold and total revenues received attributable to the IS-1 sales transactions would be summarized in an annual report filed by May 1 of each year.

2. Analysis

Since Transwestern's proposal involves the sale for resale and transportation of natural gas in interstate commerce, it is subject to our jurisdiction and the requirements of subsections (c) and (e) of section 7 of the Natural Gas Act.

Transwestern states that its application for approval of its interruptible sales program will afford it the same opportunity to pursue obtaining a portfolio of markets as is being afforded its customers in obtaining a portfolio

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[44] 18 C.F.R. § 284.106(a) and (c) (1987).

of supply. Transwestern asserts that approval of its interruptible sales program will provide Transwestern with an additional tool to aggressively market natural gas and to provide reliable cash flow to producers, thereby enhancing Transwestern's ability to negotiate market responsive contracts and settle current contract disputes with its producers. Finally, Transwestern asserts that its proposal will facilitate the growth of a competitive natural gas market by allowing gas to flow freely to any party desiring to purchase such gas, thus eliminating geographical and regulatory barriers. We agree with Transwestern's conclusions. Accordingly, we will authorize Transwestern's new rate schedule and issue a certificate, with appropriate conditions, for the proposed services.

Several intervenors are concerned that issuance of a blanket certificate for interruptible sales could lead to undue discrimination. However, Transwestern's IS rate schedule is similar to the rate schedule approved in *Northern Natural Gas Company*.[45] In that order, the Commission discussed at length the concept of a blanket interruptible sales certificate. In order to reduce the potential for undue discrimination, the Commission attached numerous conditions to that certificate. The Commission believes it appropriate to attach the same conditions to Transwestern's certificate. Accordingly, the Commission will require Transwestern to comply with four reporting requirements, which are similar to those now required of pipelines that perform self-implementing transportation under Part 284 of the regulations.

First, within 30 days after commencing each of the interruptible sales and transportation services authorized by this order, Transwestern shall file an initial report, signed under oath by a senior official, consisting of an original and five conformed copies containing a descrip-

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[45] 42 FERC ¶ 61,303 (March 11, 1988) (Docket No. CP88-2-000).

tion of the sales service, including the following information:

(1) The identities of the parties;

(2) The dates of commencement and projected termination of the service;

(3) The estimated total and maximum daily quantities of the natural gas to be sold or transported incident to a direct sale for each 12-month period commencing on the date of actual delivery;

(4) The ultimate delivery point of the gas;

(5) The price; and

(6) The WACOG included in the price.

Second, Transwestern shall amend any report filed to reflect any material change in the pertinent sales arrangement, in the same manner described above, within 30 days of the changed circumstances.

Third, not later than May 1 of each year, Transwestern shall file an annual report that contains, for each of these interruptible sales and transportation services provided during the preceding calendar year under authority of this order, the following information for each month:

(1) the total volumes sold or transported incident to direct sales;

(2) the total revenues received;

(3) the total rate charged;

(4) The WACOG included in the rate charged for each transaction;

Fourth, not later than 30 days after the termination of any sale authorized by the certificate, Transwestern shall file a report including the following information:

(1) the total volumes sold or transported incident to a direct sale under the arrangement;

(2) the total revenues received;

(3) the total rate charged;

(4) the WACOG included in the rate charged;

(5) a statement certifying that the service was provided under the terms and conditions previously reported.

To guard further against potential undue preference, should Transwestern undertake to make a sale to an affiliate, we will require Transwestern to file with the Commission the following information prior to any such sale;

(1) the name of the buyer;

(2) the buyer's location (city and state);

(3) Transwestern's affiliation with the buyer of the gas and the identity, title, mailing address, and phone number of the person(s) to contact concerning the sales and/or transportation arrangement;

(4) the nature of the involvement of the Transwestern affiliate in the transaction, *e.g.*, brokerage, transportation, purchase for consumption.

(5) the term of the sale;

(6) the estimated total and maximum daily quantities of natural gas to be sold by Transwestern; and

(7) the maximum sales rate, minimum rate, and the rate to be charged during the billing period.

The Commission will review the filing for compliance with the terms of this authorization and issue a public notice within 30 days thereafter. Upon issuance of the notice, Transwestern may commence the proposed service. Interested parties will have 30 days from the is-

suance of the notice to protest the service. If a protest is filed, Transwestern may continue to render the service for 120 days from the date of commencement or until an order terminating the service is issued, whichever is earlier. However, if no protest is filed, or if the Commission denies a timely filed protest, the service may continue until the underlying contract expires. To further protect against undue discrimination or preference, if during any billing period Transwestern charges a rate that is less than the maximum rate, within 15 days of the close of the billing period, we will require Transwestern to file the information required by the prior notice procedures outlined above, except that for item (7) it must provide the rate actually charged. This requirement will allow Transwestern the flexibility and sensitivity to market conditions needed to commence the sales in a timely manner, but will also allow us to monitor the program for prohibited preferences. Moreover, to prevent this requirement from being burdensome, if Transwestern makes a discounted sale to an affiliate, then it need only file a notice stating the extent to which the transaction changed since the prior notice was filed.

Citizen's Energy Corporation and Citizen's Gas Supply Corporation are concerned that the certificate would authorize Transwestern to broker its capacity on third-party pipelines. The certificate will not include that authority.

PSI and Natural Gas Clearinghouse, Inc. contend that the proposal would be unduly discriminatory to marketers. Hadson also requested that IS sales be made available to marketers. In addition, Natural Gas Clearinghouse, Inc. suggested that Transwestern be required to state its intention not to discriminate, to be considered an affiliated marketer for the purposes of IS-1 sales, and to give equal treatment to interruptible sales and transportation for purposes of capacity allocation and curtailment. Texaco expressed concern that discounted rates

might be difficult to detect and that IS sales customers might get preferential treatment in scheduling or curtailment. Finally, KP&L is concerned that the IS-1 rates are being discounted at the expense of interruptible transportation, and that firm sales customers would be the victims of unduly discriminatory rates.

We will condition the certificate to preclude Transwestern from giving undue preferences to off-system customers by requiring Transwestern to offer the IS service to on-system customers with the same terms and conditions available to off-system customers. The IS rate schedule must be available to an on-system customer regardless of whether that customer has satisfied any minimum purchase obligation it may have under any other Transwestern sales rate schedule. To prevent undue discrimination against on-system firm customers, we will require that the rate for the IS rate schedule shall be set at the WACOG plus variable costs of Transwestern's rate to its small firm customers.

Further, we will attach certain additional conditions to the certificate. First, marketers will be eligible to purchase gas under the IS rate schedule. Second, Transwestern must continue to hold a blanket certificate under Subpart G of Part 284, as long as the proposal is in effect. Third, if Transwestern discounts the nongas component of the IS-1 rate schedule it must also offer to discount its transportation rate under the ITS rate schedule. Fourth, Transwestern shall provide a monthly list of IS sales rates charged to all customers.

Transwestern shall be precluded from providing any undue preference in scheduling, allocation, or curtailment to sales service authorized under this certificate. Sales under the IS rate schedule shall be treated for these purposes in accordance with the same procedures used for Transwestern's other interruptible sales or transportation transactions. However, because the sales are being

made from gas that is surplus to Transwestern's requirements and are being made on an interruptible basis, it would not be practical to treat these sales as being within the scope of Transwestern's end-use curtailment plan.

ANR Pipeline Company and Colorado Interstate Gas Company request that we either dismiss this application or hold it in abeyance pending a Commission rulemaking proceeding to address whether blanket sales proposals are appropriate. We have already crossed that bridge in the *Northern Natural* case. We will not shield pipelines from the forces of competition or from the evolving natural gas market.

Since only existing facilities would be utilized to provide the sales services, approval of this proposal does not constitute a major federal action significantly affecting the quality of the human environment.

The Commission orders:

(A) The requests for hearing of SoCal and CPUC and the requests for dismissal filed by ANR and CIG are denied.

(B) In Docket No. CP88-143-000, a certificate of public convenience and necessity is issued to Transwestern authorizing it to institute a Gas Supply Inventory Charge, as more fully described above, subject to the following conditions:

1. The nomination time frame under the GIC shall be 45 days for the annual commitments and 30 days for the quarterly commitments;

2. Transwestern shall revise its tariff sheets to remove any exculpatory language concerning its obligation to furnish gas supplies under the GIC and shall include language therein warranting the security of such supplies except by reason of *force majeure*;

3. Transwestern may not impose an exit fee in the event a customer nominates zero volumes under the GIC and may not recover take-or-pay prepayment, buyout or buydown costs incurred after the date this certificate is accepted other than through the GIC mechanism;

4. The WACOG for Transwestern's Rate Schedule SG and RW customers shall be set at the lower of Transwestern's WACOG in its current PGA in effect on the date it accepts this certificate or the WACOG to be charged under the GIC, and the floor price to be charged under Transwestern's interruptible sales service under Rate Schedule IS-1 shall reflect the WACOG included in the rate to be charged Transwestern's Rate Schedule SG and RW customers.

5. Transwestern may recover its Unrecovered Purchased Gas Costs in Account No. 191 by direct billing as set forth in the text above;

6. Transwestern may only reinstate its PGA by complying with section 154.303(b) of the regulations or by establishing its right to a waiver therefrom.

7. Section 157.20(a) of the regulations shall not apply and Transwestern shall notify the Commission within 45 days if it accepts its GIC certificate and shall file changes to its tariff removing its PGA clause and making other necessary conforming changes within this same 45-day period.

(C) In Docket No. CP88-100-000, Transwestern is hereby given permission to abandon sales services not nominated under the GIC authorized in paragraph (B) above, as requested in the application in Docket No. CP88-100-000, and as more fully described above and incorporated herein by reference; and

(D) Transwestern shall file any necessary revision to its tariff within 15 days after the effective date of any

permanent abandonment of a customer's level of contract demand entitlement, as authorized in paragraph (C) above.

(E) In Docket No. CP88-99-000, a certificate of public convenience and necessity is issued to Transwestern authorizing the sale of natural gas pursuant to Rate Schedule IS-1, the blanket interruptible sales for resale to on-system and off-system customers, and the blanket transportation of natural gas incident to any direct sale made under this program, as is more fully described above, subject to the following conditions:

1. Marketers must be able to purchase gas under the IS-1 rate schedule, provided that any such marketer has the necessary certificate authority in order to make sales for resale of such gas;

2. Purchases under the IS-1 rate schedule cannot be tied to any minimum purchase obligations under any other Transwestern sales rate schedule;

3. If Transwestern discounts the nongas component of the IS-1 rate schedule it must also offer to discount its transportation rate under the ITS rate schedule;

4. The maximum rate for the IS rate schedule must equal the 100 percent load factor rate for Transwestern's CDQ-1 rate schedule and the minimum rate equal the WACOG plus variable costs included in the SG rate schedule;

5. Transwestern must adhere to the notice procedures, discounted rate filings, and various reports, all of which are described more fully above and incorporated herein by reference;

6. Transwestern must treat sales under the IS rate schedule the same as any other interruptible sales or transportation service for the purpose of

scheduling, allocating capacity, or curtailing service as more fully described above and incorporated here by reference; and

7. Transwestern must comply with Parts 154 and 155, and subsections (a) and (e) of section 157.20 of the regulations.

(F) The authorizations granted herein expire if Transwestern receives Commission authority to abandon its Part 284 Subpart G blanket transportation certificate.

APPENDIX A

Timely Interventions in Docket No. CP88-99-000

El Paso Natural Gas Company

Pacific Gas and Electric Company

Southern California Gas Company

Southern Union Gas Company

Citizens Energy Corporation and Citizens Gas Supply Corporation

Public Utilities Commission of the State of California

Producer Associations

Chevron U.S.A., Inc.

Transcontinental Gas Pipe Line Corporation

Texaco Producing Inc.

Southwest Gas Corporation

PSI, Inc.

Kansas Power and Light Company

ANR Pipeline Company and Colorado Interstate Gas Company

Tenneco Oil Company

Natural Gas Clearing House Inc.

Southern California Edison Company

APPENDIX B

Timely Interventions in Docket No. CP88-100-000

El Paso Natural Gas Company

Pacific Gas and Electric Company

Southern California Gas Company

The Producer Associations

Citizens Gas Supply Corporation

Chevron U.S.A., Inc.

Tenneco Oil Company

Southwest Gas Corporation

Southern Union Gas Company

PSI, Inc.

Kansas Power and Light Company

California Public Utilities Commission

APPENDIX C

Parties Filing Statements of Position

Transwestern Pipeline Company
Southern California Gas Company
California Public Utilities Commission
Williams Natural Gas Company
San Diego Gas and Electric Company
Kansas Power and Light Company
Pacific Gas and Electric Company
Natural Gas Clearing House, Inc.
Hadson Gas Systems, Inc.
PSI, Inc.
Exxon Corporation
ANR Pipeline Company
Colorado Interstate Gas Company
Southern Natural Gas Company

APPENDIX D

Transwestern Reserve Location

State	*County*	*Volume (Bcf)*
Texas	Hansford	20.203
	Hemphill	16.617
	Lipscomb	55.327
	Ochiltree	29.252
	Pecos	228.947
	Reeves	76.378
	Ward	21.535
	Winkler	82.900
	Others	33.294
Total Texas		564.453
New Mexico	Chaves	105.645
	Eddy	117.101
	Lea	136.913
	Roosevelt	28.933
Total New Mexico		388.592
Oklahoma	Beaver	29.752
	Custer	19.504
	Roger Mills	97.222
	Others	34.384
Total Oklahoma		180.862
Total Transwestern Reserves		1,133.907

Source: Transwestern Pipeline Company 1987 Form No. 15.

APPENDIX E

Reserves and Production in Transwestern's Supply Area
(Volumes in Bcf)

Area			*1986*	*1985*	*1984*	*1983*	*1982*
4 COUNTIES in NEW MEXICO	All Producers	Total Reserves	2,735	2,967	3,143	3,199	3,269
		Total Production	339	432	455	442	489
		Tot Prod as % Tot Res	12.4%	14.6%	14.5%	13.8%	15.0%
	Trans-western	Reserves	411	470	469	461	405
		Production	72	92	99	98	82
		TW Res as % Tot Res	15.0%	15.8%	14.9%	14.4%	12.4%
		TW Res as % Tot Prod	21.2%	21.3%	21.8%	22.2%	16.8%
13 COUNTIES in OKLAHOMA	All Producers	Total Reserves	9,274	8,947	8,466	8,709	8,583
		Total Production	926	901	895	777	813
		Tot Prod as % Tot Res	10.0%	10.1%	10.6%	8.9%	9.5%
	Trans-western	Reserves	217	211	263	252	170
		Production	35	38	50	54	50
		TW Res as % Tot Res	2.3%	2.4%	3.1%	2.9%	2.0%
		TW Prod as % Tot Prod	3.8%	4.2%	5.6%	6.9%	6.2%
6 COUNTIES in TEXAS RRD 8	All Producers	Total Reserves	5,614	5,713	6,083	6,463	6,613
		Total Production	465	489	527	568	669
		Tot Prod as % Tot Res	8.3%	8.6%	8.7%	8.8%	10.1%
	Trans-western	Reserves	588	770	612	639	676
		Production	42	46	60	76	103
		TW Res as % Tot Res	10.5%	13.5%	10.1%	9.9%	10.2%
		TW Prod as % Tot Prod	9.0%	9.4%	11.4%	13.4%	15.4%

APPENDIX E—Continued

Area			*1986*	*1985*	*1984*	*1983*	*1982*
10 COUNTIES in TEXAS RRD 10	All Producers	Total Reserves	3,893	3,858	4,037	4,113	4,366
		Total Production	386	399	444	467	534
		Tot Prod as % Tot Res	9.9%	10.3%	11.0%	11.4%	12.2%
	Trans-western	Reserves	179	270	214	255	287
		Production	24	41	47	56	58
		TW Res as % Tot Res	4.6%	7.0%	5.3%	6.2%	6.6%
		TW Prod as % Tot Prod	6.2%	10.3%	10.6%	12.0%	10.9%
TOTAL TRANS-WESTERN SUPPLY AREAS	All Producers	Total Reserves	21,516	21,485	21,729	22,484	22,831
		Total Production	2,116	2,221	2,321	2,254	2,505
		Tot Prod as % Tot Res	9.8%	10.3%	10.7%	10.0%	11.0%
	Trans-western	Reserves	1,395	1,721	1,558	1,607	1,538
		Production	173	217	256	284	293
		TW Res as % Tot Res	6.5%	8.0%	7.2%	7.1%	6.7%
		TW Prod as % TW Res	12.4%	12.6%	16.4%	17.7%	19.1%
		TW Prod as % Tot Prod	8.2%	9.8%	11.0%	12.6%	11.7%
		TW Prod as % Tot Res	0.8%	1.0%	1.2%	1.3%	1.3%

Source: DOE/EIA Form 23

AREA	
NEW MEXICO (East)	TOTAL RESERVES—all producers DEDICATED RES—all jurisdictional P/L TRANSWESTERN DEDICATED RES COMMITTED RES—Category I & II producers UNCOMMITTED RES—Category I & II producers TOTAL RES—Category I & II producers DEDICATED RES as % of TOTAL RES COMMITTED RES as % CATEGORY I & II RES
OKLAHOMA	TOTAL RESERVES—all producers DEDICATED RES—all jurisdictional P/L TRANSWESTERN DEDICATED RES COMMITTED RES—Category I & II producers UNCOMMITTED RES—Category I & II producers TOTAL RES—Category I & II producers DEDICATED RES as % of TOTAL RES COMMITTED RES as % CATEGORY I & II RES
TEXAS RRD 8	TOTAL RESERVES—all producers DEDICATED RES—all jurisdictional P/L TRANSWESTERN DEDICATED RES COMMITTED RES—Category I & II producers UNCOMMITTED RES—Category I & II producers TOTAL RES—Category I & II producers DEDICATED RES as % of TOTAL RES COMMITTED RES as % CATEGORY I & II RES
TEXAS RRD 10	TOTAL RESERVES—all producers DEDICATED RES—all jurisdictional P/L TRANSWESTERN DEDICATED RES COMMITTED RES—Category I & II producers UNCOMMITTED RES—Category I & II producers TOTAL RES—Category I & II producers DEDICATED RES as % of TOTAL RES COMMITTED RES as % CATEGORY I & II RES
TOTAL U.S. Less Alaska	TOTAL RESERVES—all producers DEDICATED RES—all jurisdictional P/L COMMITTED RES—Category I & II producers UNCOMMITTED RES—Category I & II producers TOTAL RES—Category I & II producers DEDICATED RES as % of TOTAL RES COMMITTED RES as % CATEGORY I & II RES
TOTAL TRANS-WESTERN SUPPLY AREA	TOTAL RESERVES—all producers DEDICATED RES—all jurisdictional P/L TRANSWESTERN DEDICATED RES COMMITTED RES—Category I & II producers UNCOMMITTED RES—Category I & II producers TOTAL RES—Category I & II producers DEDICATED RES as % of TOTAL RES COMMITTED RES as % CATEGORY I & II RES

Source: DOE/EIA 0167, 0126 (77-86)

western Pipeline Company's Supply Area (Bcf)

1986	*1985*	*1984*	*1983*	*1982*	*1981*	*1980*	*1979*	*1978*	*1977*
2,982	3,310	3,492	3,537	3,705	3,876	3,799	4,306	3,899	3,848
2,822	2,972	3,057	3,159	3,336	3,609	3,105	3,197	3,296	3,127
411	470	469	461	405	421	292	269	275	275
Not Reported		2,878	2,983	3,146	3,160	3,333	3,493	3,385	3,479
Not Reported		52	65	54	50	68	38	26	25
		2,930	3,048	3,200	3,210	3,401	3,531	3,411	3,504
94.6%	89.8%	87.5%	89.3%	90.0%	93.1%	81.7%	74.2%	84.5%	81.3%
S		98.2%	97.9%	98.3%	98.4%	98.0%	98.9%	99.2%	99.3%
17,779	17,078	17,102	17,261	17,140	15,507	13,908	14,545	14,417	13,889
7,688	8,535	9,233	9,777	10,230	8,577	9,125	8,208	7,796	7,394
217	211	263	252	170	201	126	67	32	34
Not Reported		11,360	10,994	10,653	10,253	9,905	10,014	10,909	10,197
Not Reported		608	445	437	436	288	214	193	247
		11,968	11,439	11,090	10,689	10,193	10,228	11,102	10,444
43.2%	50.0%	54.0%	56.6%	59.7%	55.3%	65.6%	56.4%	54.1%	53.2%
S		94.9%	96.1%	96.1%	95.9%	97.2%	97.9%	98.3%	97.6%
8,330	8,250	8,294	9,078	8,992	9,250	9,785	10,718	11,093	11,728
2,818	3,188	2,972	2,999	3,069	3,152	3,397	3,801	4,161	4,691
588	770	612	639	676	675	831	930	995	1,021
Not Reported		7,473	7,883	8,008	8,089	8,568	9,219	9,367	10,293
Not Reported		187	127	104	160	441	471	398	64
		7,660	8,010	8,112	8,249	9,009	9,690	9,765	10,357
33.8%	38.6%	35.8%	33.0%	34.1%	34.1%	34.7%	35.5%	37.5%	40.0%
S		97.6%	98.4%	98.7%	98.1%	95.1%	95.1%	95.9%	99.4%
5,857	6,044	6,060	6,485	6,731	6,720	6,927	7,289	7,406	7,744
2,859	3,027	3,305	3,623	3,843	5,069	4,447	4,861	5,189	5,020
179	270	214	255	287	292	303	271	244	241
Not Reported		4,112	4,334	5,179	4,974	5,273	5,681	5,944	6,216
Not Reported		556	480	489	573	543	555	495	584
		4,668	4,814	5,668	5,547	5,816	6,236	6,439	6,800
48.4%	50.1%	54.5%	55.9%	57.1%	75.4%	64.2%	66.7%	70.1%	64.8%
S		88.1%	90.0%	91.4%	89.7%	90.7%	91.1%	92.3%	91.4%
167,754	167,979	171,508	174,755	174,252	176,385	175,864	176,060	175,988	175,196
80,602	85,102	89,894	94,498	98,711	98,339	97,102	97,299	93,993	92,889
Not Reported		121,625	126,308	131,583	133,015	133,680	139,241	142,601	144,684
Not Reported		12,655	10,851	9,691	11,351	9,786	9,022	8,825	8,216
		134,280	137,159	141,274	144,366	143,466	148,263	151,426	152,900
48.0%	50.7%	52.4%	54.1%	56.6%	55.8%	55.2%	55.3%	53.4%	53.0%
S		90.6%	92.1%	93.1%	92.1%	93.2%	93.9%	94.2%	94.6%
34,948	34,682	34,948	36,361	36,568	35,353	34,419	36,858	36,815	37,209
16,187	17,722	18,567	19,558	20,478	20,407	20,074	20,067	20,442	20,232
1,395	1,721	1,558	1,607	1,538	1,589	1,552	1,537	1,563	1,571
Not Reported		25,823	26,194	26,986	26,476	27,079	28,407	29,605	30,185
Not Reported		1,403	1,117	1,084	1,219	1,340	1,278	1,112	920
		27,226	27,311	28,070	27,695	28,419	29,685	30,717	31,105
46.3%	51.1%	53.1%	53.8%	56.0%	57.7%	58.3%	54.4%	55.5%	54.4%
S		94.8%	95.9%	96.1%	95.6%	95.3%	95.7%	96.4%	97.0%

APPENDIX G

Table 6. Estimated Surplus Natural Gas

Date Surveyed	Volume Estimated as Available During Six-Month Period [a] (Bcf)	Amount and Percent of Estimated Volume from Canadian Sources		Period During Which Surplus Deliverability Available
		Volume (Bcf) [b]	Percent	
1982				
January	456	35	8	January 1982—June 1982
April	864	107	12	April 1982—September 1982
July	1,229	99	8	July 1982—December 1982
October	1,189	80	7	October 1982—March 1983
1983				
January	1,715	176	10	January 1983—June 1983
April	2,605	243	9	April 1983—September 1983
July	2,357	110	5	July 1983—December 1983
October	2,077	127	6	October 1983—March 1984
1984				
January	1,695	154	9	January 1984—June 1984
April	1,897	108	6	April 1984—September 1984
July	1,872	202	11	July 1984—December 1984
October	1,506	117	8	October 1984—March 1985
1985				
January	1,650	161	10	January 1985—June 1985
April	1,896	139	7	April 1985—September 1985
July	1,752	174	10	July 1985—December 1985
October	1,535	158	10	October 1985—March 1986

TABLE 6—Continued

Date Surveyed	Volume Estimated as Available During Six-Month Period[a] (Bcf)	Amount and Percent of Estimated Volume from Canadian Sources		Period During Which Surplus Deliverability Available
		Volume (Bcf)[b]	Percent	
1986				
January	1,653	165	10	January 1986—June 1986
April	2,158	196	9	April 1986—September 1986
July	2,283	160	7	July 1986—December 1986
October	1,974	177	9	October 1986—March 1987
1987				
January	1,693	151	9	January 1987—June 1987
April	1,828	155	8	April 1987—September 1987
July	1,782	142	8	July 1987—December 1987
October	1,594	143	9	October 1987—March 1988
1988				
January	1,620	130	8	January 1988—June 1988

[a] The total estimated volume of surplus natural gas available during the six-month periods may include some double counting. For example, if a pipeline company purchasing gas from a first supplier reports all gas in excess of system customer requirements as surplus, this pipeline company could have a contract with another company which is taking less than 100 percent of the contract quantity. Inasmuch as the second company has contract rights to the gas, it could report this same gas as surplus. Every effort to eliminate or minimize these occurrences has been effected.

[b] The volume from Canadian sources is included in the total estimated surplus.

Notes and Sources: See the last page of this section.

Reproduced from: EIA, *Natural Gas Monthly* (Jan. 1988)

FEDERAL ENERGY REGULATORY COMMISSION

Docket Nos. CP88-99-000, CP88-99-001, CP88-100-000, and CP88-143-000

TRANSWESTERN PIPELINE COMPANY

ORDER GRANTING REHEARING IN PART AND CLARIFYING PRIOR ORDER

(Issued July 29, 1988)

Before Commissioners: Martha O. Hesse, Chairman; Anthony G. Sousa, Charles G. Stalon and Charles A. Trabandt.

Background

On December 1, 1987, Transwestern Pipeline Company (Transwestern) submitted three interrelated filings. In Docket No. CP88-143-000,[1] Transwestern proposed to establish a Gas Supply Inventory Charge (GIC) which it purported to be in compliance with the guidelines established in Order No. 500.[2] In Docket No. CP88-100-000, Transwestern proposed to abandon its firm sales obligation to the extent that obligation exceeded customer nominations under the GIC. In Docket No. CP88-99-000, Transwestern proposed to establish an on-system and off-system interruptible sales (IS) service with pregranted authority to abandon this service.

By order,[3] issued May 11, 1988, the Commission determined that no material disputed factual issues existed

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[1] Initially docketed as Docket No. RP88-35-000.

[2] *FERC Statutes and Regulations* ¶ 30,761 (1987).

[3] 43 FERC ¶ 61,240 (1988).

and that the Commission could evaluate Transwestern's proposal without the need for a hearing. The Commission further determined that Congress afforded it flexibility in selecting a methodology to determine just and reasonable rates [4] and that with regard to the GIC, a departure from the traditional cost-of-service review was warranted.

In its May 11, 1988 order, the Commission determined that Southern California Gas Company (Southern California), which would be Transwestern's sole remaining potential large customer if the GIC were implemented, had alternative sources of supply available, and that these alternative competitive sources, including other interstate pipelines and gas producers, would act as a restraint on Transwestern's prices. The Commission found that because Southern California is not a captive customer and is a sophisticated buyer in the gas market, Transwestern would be required to keep its gas costs as low as possible to retain Southern California's business. The Commission found that Transwestern had already taken steps to reduce its gas costs by purchasing market responsive gas and renegotiating its problem contracts.

The Commission found that the competitive conditions in the southern California market in which Transwestern and Southern California operate warranted consideration of the GIC proposal with a lightened regulatory hand and approved it, subject to certain conditions designed to enhance the effect of the competitive forces and to otherwise conform the proposal to Commission policy. The Commission also approved Transwestern's corresponding application in Docket No. CP88-100-000 (which was unopposed) to abandon its firm sales obligation to the extent that obligation exceeded customer nominations under the GIC. Finally, the Commission approved Transwestern's IS

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[4] *Citing Permian Basin Area Rate Cases*, 390 U.S. 747, 790 (1968).

service, in its May 11, 1988 order, which would be furnished using system supply in excess of Transwestern's firm customers' requirements.

On June 9, 1988, the Public Utilities Commission of the State of California (CPUC) filed a request for clarification and rehearing of the Commission's May 11, 1988 order. On June 10, 1988, rehearing requests were filed separately by the Producer Associations, Pacific Gas and Electric Company (PG&E), Kansas Power and Light Company (Kansas Power), Southern California, and Transwestern, and jointly by ANR Pipeline Company and Colorado Interstate Gas Company (together, ANR). The rehearing requests of Southern California and Transwestern embrace requests for clarification. Williams Natural Gas Company (Williams) filed a request for clarification on June 10, 1988. The merits of the parties respective positions are addressed below.

Discussion

A. GIC

1. Need for hearing.

CPUC, PG&E and Kansas Power argue that the Commission erred in approving the GIC without an evidentiary hearing. PG&E notes that a hearing was ordered in other GIC proposals[5] pending before the Commission and complains that the Commission's refusal to grant the numerous requests for hearing in this proceeding is arbitrary and capricious. PG&E contends that a number of material factual issues are in dispute and that a hearing is necessary to decide them. For instance, PG&E contends, a hearing is necessary to determine the scope of

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[5] *Citing Natural Gas Pipeline Company of America*, 43 FERC ¶ 61,068 (1988); *El Paso Natural Gas Co.*, 42 FERC ¶ 61,092 (1988); *Northwest Pipeline Corporation*, 42 FERC ¶ 61,019 (1988); and *Texas Eastern Transmission Corporation*, 41 FERC 61,373 (1987). CPUC also raises this issue.

Transwestern's supply obligation to its customers, the extent to which Transwestern's gas costs can be reduced by requiring it to adopt least-cost purchasing practices, the purported similarity between the GIC and minimum take provisions eliminated in Order No. 380-C [6] and whether the GIC reflects Transwestern's actual cost of maintaining gas supplies for its customers.

CPUC and Kansas Power contend that a hearing is necessary to determine whether the GIC is cost-based, as contended by Transwestern.[7] CPUC and Kansas Power dispute the Commission's conclusion that the southern California market is workably competitive and argue that a hearing is necessary to compel Transwestern to produce data concerning this issue. Finally, CPUC argues that even if the Commission may lawfully base its approval of the GIC on market forces, it must nevertheless use Transwestern's cost of service as a reference point.[8]

The Commission affirms its decision to approve Transwestern's GIC without hearing. The issue raised by CPUC and Kansas Power concerning whether the relevant market is workably competitive is not a disputed factual issue. Rather, it is a legal conclusion based on their consideration of the factual evidence developed in the record. The Commission carefully considered this evidence, including the availability of gas in both southern California and in Transwestern's supply area, the relative

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[6] *FERC Statutes and Regulations* ¶ 30,607 (1984).

[7] CPUC contends, for example, that in the GIC, Transwestern assumed that it would settle take-or-pay claims for 25 cents on the dollar, whereas in actuality, Transwestern's settlement costs are less than 20 cents per dollar. Kansas Power argues that in a competitive market, prices will approximate the seller's cost basis, but that here, Transwestern's proposed GIC prices do not track its costs.

[8] *Citing Farmers Union Cent. Exchange, Inc. v. FERC*, 734 F.2d 1486, at 1502 and 1509 (1984); and *FPC v. Texaco Inc.*, 417 U.S. 380 at 399 (1974).

sophistication of Southern California as a gas purchaser and Transwestern's lack of market power over Southern California and concluded that Transwestern's customers have sufficient options to ensure that the rates charged to Southern California would be just and reasonable. CPUC and Kansas Power draw different inferences from the factual evidence than does the Commission. However, contrary to their assertions, the Commission has not recharacterized factual issues as matters of policy. To the contrary, CPUC and Kansas Power improperly seek to recast their conclusion as to the nature of competition in the relevant market as a disputed fact.

Nor has the Commission, as these parties contend, improperly evaded its statutory oversight obligation with respect to its review of the GIC by approving it solely on the basis of competitive forces. The Commission readily acknowledges that it "lacks the authority to place exclusive reliance on market prices"[9] in approving Transwestern's GIC; however, it has not done so here. As noted in the May 11, 1988 order, the Commission considered the availability of alternative supply sources other than purchases from Transwestern in concluding that Transwestern's prices under its GIC would fall within a just and reasonable range.[10] These alternatives include (1) purchases from other pipelines at rates the Commission has already found to be just and reasonable; and (2) wellhead purchases deemed to be at a just and reasonable price pursuant to section 601(b) of the Natural Gas Policy Act, plus the cost of transportation at Commission-regulated rates. The Commission found that in order to retain Southern California's business, Transwestern would be required to maintain its prices at or below the upper boundary of the zone of reasonableness represented

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[9] *FPC v. Texaco Inc.*, 417 U.S. at 400-401 (1974).

[10] *Citing Baltimore Gas and Electric Company*, 40 FERC ¶ 61,170, at p. 61,538 (1987).

by these alternative supply sources. The Commission does not read *Texaco* and *Farmers Union* as specifically requiring a cost-of-service analysis of the rates contained in Transwestern's GIC, but rather that those rates be constrained by a just and reasonable ceiling. Southern California's purchasing alternatives provide that ceiling, beneath which Transwestern must post its GIC prices if it chooses to retain Southern California as a customer. Moreover, in contrast to the general and indirect evidence of competition relied by the Commission and criticized by the court in *Farmers Union*, footnote 8, *supra*, the evidence of competition here is substantial and bears directly on conditions in the relevant geographic market.

PG&E raises several additional matters which it asserts are disputed issues of material fact requiring a hearing. The first involves the purported similarity between Transwestern's Forward Supply Service [11] and the minimum take provisions proscribed in Order No. 380-C and whether the Forward Supply Service accurately reflects its supply contracts and its duty to supply its customers. As discussed below, a hearing is not necessary to resolve this issue. The second issue raised by PG&E is whether approval of the GIC should be conditioned on the requirement that Transwestern adopt a least-cost purchasing strategy in sourcing its supply requirements. As noted in the prior order, Southern California's access to alternative sources provides incentives for Transwestern to reduce its gas costs. The Commission found that Transwestern had already taken steps to do so. In addition, as noted above, the presence of alternatives justifies a relaxation of the Commission's duty to examine cost-of-service issues such as Transwestern's gas supply costs. The Commission concludes that a hearing is not required to address this issue.

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[11] As proposed by Transwestern, Southern California would be required to nominate at least 157,500 Dth per day before being eligible to freely nominate incremental levels of service under the Option Service for quantities in excess of 157,500 Dth per day.

2. Exit fee and availability of Order No. 500 alternate passthrough mechanism.

CPUC, Southern California, Producer Associations and Transwestern raise related issues concerning the Commission's prohibition against the assessment of an exit fee in conjunction with the GIC and the extent to which the Commission will permit Transwestern to recover take-or-pay or similar costs after the GIC becomes effective. Producer Associations argues that the Commission's prohibition against an exit fee is unreasonable because Transwestern is obligated in contracts with producers to take a certain level of gas and will be required to compensate its suppliers for relief from these contractual provisions in the future.

Transwestern argues that the prohibition in Order No. 500 against recovery of future take-or-pay liability other than through a GIC mechanism does not encompass take-or-pay prepayment, buyout, buydown and contract reformation costs arising out of existing contracts, but which it has not yet incurred. Transwestern contends that the intent of Order No. 500 is to limit recovery through a GIC mechanism only to future take-or-pay liability arising from contracts entered into after the GIC is implemented, and not future liability arising out of existing contracts. Transwestern complains that its GIC is not designed to recover the cost of buying out or reforming existing contracts and argues that the Commission's order will unlawfully deprive it of an opportunity to recover prudently incurred costs. Transwestern asserts that it will not have completed the process of reforming, buying out or buying down existing contracts by the time its GIC must be accepted and argues that a reasonable transition period should be afforded for this purpose after a GIC is implemented. Transwestern states that it is now preparing a transitional filing seeking approval for use

of the Order No. 500 passthrough mechanism for its existing take-or-pay costs.[12]

Transwestern argues that in prohibiting it from recovering take-or-pay costs relating to existing contracts other than through its GIC, the Commission had improperly foreclosed its otherwise available right under Order No. 500 to file for take-or-pay costs actually paid through December 31, 1988 or known and measurable within the following nine months.[13] Transwestern contends that the Commission's action discriminates against pipelines which propose to implement GICs and runs counter to the policy of Order No. 500 to provide pipelines relief from their take-or-pay problems.

Transwestern also contends that it should be permitted to assess an exit fee to a customer (i.e., Southern California) that first opts for service under the GIC but later reduces its purchase commitment substantially. Transwestern argues that the exit fee prohibition is an unlawful attempt to condition its certificate which is unsupported by public interest considerations.

Southern California and CPUC also seek clarification that the alternative Order No. 500 passthrough mechanism is limited to recovery of take-or-pay costs which Transwestern has already incurred, and that future incurrence of such costs, even if they reflect buyout, buydown or reformation of existing contracts, can only be recovered through the GIC. CPUC argues that mere exposure of Transwestern to take-or-pay liability under existing contracts should not be recoverable other than through the GIC unless Transwestern has already set-

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[12] On June 24, 1988, in Docket No. RP88-198-000, Transwestern filed to recover up to $225 million in take-or-pay buyout and contract reformation costs, exclusive of arbitration and litigation costs.

[13] *Citing* 18 C.F.R. § 2.104(c) (1987); and *Southern Natural Gas Company*, 41 FERC ¶ 61,367 (1987).

tled these liabilities and made payments to producers or such payments are known and measurable through reference to binding settlement contracts. CPUC contends that the deadline for filing for recovery of take-or-pay costs requires actual payment or known and measurable settlement amounts, and that mere exposure to take-or-pay liability is not a valid basis for recovery.

CPUC argues that if unincurred reformation costs may be recovered outside the GIC, then Southern California's nomination choice under the GIC will be subject to uncertainty as to its future take-or-pay exposure and would be contrary to the Commission's statement in the May 11, 1988 order that Southern California know the full cost consequences of its nomination in advance and that Transwestern be prohibited from assessing an exit fee in conjunction with the GIC. CPUC further argues that if Transwestern is able to collect as yet unincurred costs apart from the GIC, Southern California would not be able to nominate zero volumes under the GIC without incurring additional future costs. CPUC contends that such a result would be inconsistent with the premise in the Commission's May 11, 1988 order that Transwestern and Southern California be placed on an equal competitive footing.

CPUC also seeks clarification as to the scope of take-or-pay costs recoverable only through the GIC. It argues that all buyout, buydown and reformation costs should be included, whether related to a take-or-pay provision, a minimum-take provision or a gas-pricing clause.[14]

The Commission's intent in the May 11, 1988 order was to limit recovery of take-or-pay costs under the alternative passthrough mechanism of Order No. 500 to costs

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[14] *Citing El Paso Natural Gas Company*, 42 FERC ¶ 61,024, at pp. 61,146 and 61,149 (1988); and *Natural Gas Pipeline Company of America*, 43 FERC ¶ 61,194 (1988); *reh'g granted in part and denied in part*, 43 FERC ¶ 61,474 (1988).

that have already been paid or which are known and measurable through reference to binding written agreements entered into before acceptance of the GIC certificate. Liability for future costs under binding written agreements with producers entered into after acceptance of the GIC certificate must be recovered through the GIC mechanism.

In its request for clarification and rehearing, Transwestern improperly equates potential future liability arising out of existing contracts with take-or-pay liability already paid or incurred under a binding agreement. Such future liability can be recovered only through the GIC mechanism while the latter may be recovered under the alternative passthrough mechanism of Order No. 500, as explained above. This interpretation of the Order No. 500 guidelines is consistent with the policy expressed therein that GICs serve as a future oriented cost-recovery mechanism. To the extent that Transwestern anticipates future liability to occur under its existing contracts, it may, before accepting its GIC certificate, negotiate the resolution of that liability with its producers, reduce its exposure to a sum certain in a binding agreement and file for recovery of such costs under the Order No. 500 alternative passthrough mechanism. Further, as noted in the prior order, GIC customers must know the full-cost consequences of their nominations. To the extent that Transwestern does not know the full-cost consequences of its GIC service because it has not yet renegotiated its supply contracts, then it is not ready to implement a GIC under the policies set forth in Order No. 500. Finally allowing Transwestern to collect take-or-pay costs from Southern California apart from the GIC would weaken the latter's competitive position, contrary to the Commission's premise in approving the proposal.

Transwestern also contends that it should be permitted to assess an exit fee if Southern California first commits to purchases under the GIC and subsequently reduces its

nominations. Transwestern's position is contrary to the Commission's policy, as expressed in Order No. 500 and in the May 11, 1988 order, that Southern California know in advance the full-cost consequences of its nomination decisions. In addition, assessment of an exit fee is inconsistent with the Commission's objective that prices under the GIC be constrained by market forces. Unascertainable future costs stemming from a potential future reduction in nominations by Southern California may not be later assessed by Transwestern under the GIC. In order to limit the risk of a supply imbalance if Southern California reduces its GIC nominations, Transwestern should seek greater flexibility in its contracts with its suppliers.

Transwestern also contends that the Commission's prohibition against an exit fee and limitation on recovery through the Order No. 500 alternative passthrough mechanism unlawfully conditions its certificate in violation of sections 4, 5, and 7 and suffers other infirmities, including a purported absence of evidentiary support and an alleged violation of its right to due process. Transwestern also observes that the Order No. 500 alternate passthrough mechanism is available for costs paid on or before December 31, 1988 or are known and measurable within the following nine months.[15] Transwestern argues that in requiring an earlier cutoff date as a condition of acceptance of its GIC, the Commission has limited this option without prior notice and arbitrarily discriminates against it vis-a-vis pipelines that will not implement a GIC before then.

The Commission finds that its position concerning the limitation restricting as yet unincurred costs to recovery through the GIC mechanism is a matter of policy applicable in general to GICs and that application of that policy here is not unreasonable, and therefore, it should

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[15] 18 C.F.R. § 2.104(c).

not be waived or modified. Imposition of the noted condition is necessary to bring Transwestern's proposal into conformity with that policy. The Commission's exercise of its conditioning power is not unreasonable because, as Transwestern itself notes, it can reduce its potential future liability under its existing contracts by entering into definitive agreements with producers before accepting its GIC certificate in order to preserve its right to file under the alternate passthrough mechanism permitted by Order No. 500, or alternatively, defer implementation of a GIC. Moreover, Transwestern had explicit notice in Order No. 500 that the GIC would be the sole mechanism for recovery of future take-or-pay costs. Transwestern's position is rejected.

CPUC and Southern California also seek clarification as to the types of take-or-pay costs which would be limited to recovery only through the GIC. Their position on this issue is correct. The costs so limited include buyout and buydown costs, as well as contract reformation costs related to take-or-pay provisions, minimum take provisions or a gas pricing clause. Such costs also include prepayments under take-or-pay contracts. Prepayments incurred by pipelines which have adopted a GIC are no longer to be considered a working capital item entitled to be included in rate base to earn a rate of return.[16] Transwestern's request for clarification is denied and the requests for clarification of Southern California and CPUC are granted to the extent they are consistent with the analysis above.

3. Direct billing of Account No. 191 costs.

As noted, the Commission's May 11, 1988 order provided for the direct billing (or refund) of undercollections (overcollections) to clear Transwestern's unrecov-

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[16] Nor are prepayments recoverable under the alternative Order No. 500 passthrough mechanism. *Tennessee Gas Pipeline Company*, 42 FERC 61,175 at 61,627-28 (1988).

ered purchased gas cost account upon termination of its PGA and institution of the GIC. A number of parties seek rehearing or clarification of this determination. CPUC states that it does not object to direct billing of undercollections arising as a result of accounting errors, but complains that pipelines characteristically settle billing disputes with producers concerning applicable gas prices at the same time they negotiate relief from take-or-pay liability. If Transwestern is allowed to directly bill all of its unrecovered purchased gas costs, CPUC argues, there is a potential for Transwestern to either bargain less forcefully regarding its billing discrepancies with producers or to agree to a suboptimal billing settlement in favor of obtaining concessions in take-or-pay negotiations. In order to foreclose this perceived potential for abuse, CPUC proposes to subject billing disputes to the same Order No. 500 passthrough mechanism (i.e., coequal absorption through a demand charge) available for recovery of take-or-pay costs. CPUC also argues that the direct billing mechanism approved for Account No. 191 costs removes incentives for pipelines to contain their gas costs. CPUC also complains that no time limit is placed on the recovery through direct billing of Transwestern's Account No. 191 costs, thereby creating the potential for misallocation of settlement costs to the pre-GIC period for billing disputes arising after the GIC is implemented. CPUC recognizes that parties have the right to challenge inclusion of improper amounts in Account No. 191 but complains that scrutiny of all of Transwestern's settlements would be time consuming and burdensome. It requests that the Commission limit direct billing to costs incurred before Transwestern accepts its GIC certificate.

Southern California likewise objects to the Commission's failure to impose a time limit on the incurrence of Account No. 191 costs after the date of implementation of the GIC and specifically requests clarification that it

has the right to challenge the prudence and reasonableness of costs that would be directly billed to it by Transwestern. Williams seeks clarification that any Account No. 191 amounts directly billed by Transwestern may be passed through in its PGA filing in the same manner as Transwestern's charges have previously been flowed through in its rates.

Kansas Power and PG&E oppose direct billing of Account No. 191 balances on the grounds that it constitutes retroactive ratemaking. PG&E argues that the affected Transwestern customers lacked notice as to the future assessment of a direct bill to close out Account No. 191 and points out that these customers' purchasing choices may have been affected by knowledge of the future surcharge. Kansas Power argues in addition that Transwestern's PGA should not be a mechanism to match unrecovered costs to specific customers [17] and that the appropriate method for Transwestern to clear this account is by itself absorbing any uncollected balance.[18] Both Kansas Power and PG&E contend that direct billing is an extraordinary remedy which the Commission has not adequately supported.

The Commission finds that direct billing is justified because Transwestern will be closing out its Account No. 191 and instituting a new service under its GIC. To require Transwestern to absorb potential undercollections related to gas purchases made before implementation of the GIC would be unreasonable because there is no showing that the costs at issue have been imprudently or abusively incurred.

The contention of Kansas Power and PG&E that direct billing constitutes retroactive ratemaking is rejected.

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[17] *Citing Kentucky West Virginia Gas Company,* 37 FERC ¶ 61,310 (1986).

[18] *Citing Tennessee Gas Pipeline Company,* 33 FERC ¶ 61,006 and ¶ 61,061 (1985).

Here, Transwestern's customers had adequate notice that they would pay Transwestern's actual gas costs through operation of the surcharge component of the PGA mechanism. However, the PGA will be terminated on Transwestern's acceptance of its GIC certificate, and recovery of undercollections through the surcharge component obviously would not be feasible. Direct billing serves as an appropriate surrogate for recovery through the surcharge component. Moreover, even if the Commission were to accept, *arguendo*, that direct billing of possible undercollections constitutes retroactive ratemaking, the Commission has power to waive the filed rate doctrine.[19] The circumstances in this case would warrant exercise of that waiver power, assuming that any waiver is necessary, for use of direct billing as a transitional mechanism which aligns cost recovery to cost causation. The cases cited by Kansas Power which permitted certain pipeline customers to limit or avoid cost responsibility by reducing or ceasing sales service between PGA billing periods are distinguishable because they involve continued operation of the PGA billing mechanism in the pipelines' rate structure rather than termination of that mechanism, as is the case here.

The Commission is persuaded, however, that in order to promote certainty as to the total amount of costs which may be directly billed and to remove a potential source of abuse in settlement negotiations between Transwestern and its suppliers, a time limit should be imposed on the incurrence of directly billable undercollections. Transwestern will be permitted to bill its customers for unrecovered Account No. 191 costs actually paid or incurred (or, in the case of billing dispute settlements, amounts that are known and measurable through reference to binding written agreements) within six months after the date Transwestern accepts its GIC. This should

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[19] *See, e.g., Columbia Gas Transmission Corporation v. FERC*, 844 F.2d 879, 880 (D.C. Cir. 1988).

afford Transwestern sufficient time to reconcile its accounts with producers and will provide an incentive for Transwestern to resolve promptly any billing disputes. The proposal of CPUC to limit recovery through direct billing to amounts incurred by Transwestern prior to acceptance of its GIC certificate is unreasonable because Transwestern will not know the extent of undercollections until after the PGA is terminated, and, accordingly is rejected. Transwestern is also required to flow through only refunds it receives from its suppliers applicable to purchases before the effective date of the GIC.

Williams has requested clarification as to the method by which it can recover any directly billed amounts from its customers. The Commission concludes that undercollections should be billed through its PGA surcharge mechanism. Since Williams' PGA will not be terminated, direct billing to its customers of amounts directly billed by Transwestern is inappropriate. Finally, Southern California seeks clarification of its right to challenge the prudence and reasonableness of amounts which Transwestern may seek to directly bill it. The Commission affirms Southern California's rights in this regard.

4. Similarity of the GIC to minimum bill and minimum take provisions.

Kansas Power, PG&E and CPUC challenge the Forward Supply Service [20] component of the GIC as violative of the Commission's policy, promulgated in Order No. 380-C, prohibiting pipeline tariff provisions which require customers to take specified minimum quantities of gas. In addition, PG&E and CPUC contend that the

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[20] Customers would be required to nominate the entire quantity, i.e., 157,500 Dth per day, of Forward Supply Service before being eligible to nominate incremental quantities under the Option Service (levels above 157,500 Dth per day).

cost level[21] established in the Forward Supply Service is unreasonable and restricts implementation of least-cost purchasing strategies by customers.

The Commission recognizes certain similarities between the minimum take provisions proscribed in Order No. 380-C and the Forward Supply Service proposed in Transwestern's GIC. However, as discussed below, the premise underlying the Commission's prohibition against minimum-take clauses does not exist here, and, accordingly, the Commission will not require modification of the Forward Supply component of Transwestern's GIC.

In Order No. 380-C, the Commission reasoned that minimum take provisions caused customers to purchase gas they would not otherwise take, causing these customers to incur unnecessary costs.[22] In addition, the Commission found that minimum-take provisions, like minimum commodity bills, act as a restraint on competition because pipelines and the producers remain artificially insulated from market risk.[23] In the instant case, Southern California's nomination of volumes under the GIC is a voluntary reflection of its decision to maintain Transwestern as a supplier. The Commission has previously determined that the relevant market is competitive, that Transwestern lacks market power, and that Southern California's access to alternative supplies constrains anticompetitive conduct by Transwestern. Accordingly, the Commission finds that the ills Order No. 380-C was designed to cure are here inapplicable and, therefore, that order cannot serve as a basis for our outright rejection of this aspect of the proposal. Nor is the

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[21] Transwestern has structured the GIC on a declining cost basis, i.e., a customer would be required to accept Transwestern's most expensive supplies first before obtaining access through GIC nominations to Transwestern's successively less expensive supplies.

[22] *FERC Statutes and Regulations* ¶ 30,607, at p. 31,183 (1984).

[23] *Id.*

Commission, in declining to expressly prohibit a GIC feature which requires a customer to nominate a purchase quantity greater than or equal to a specified level, positing that such a feature is necessary or desirable here or approving any specific provision in Transwestern's GIC proposal. Rather, in view of the competitive environment in which Southern California exists as a potential buyer and Transwestern stands as a potential seller, the Forward Supply Service component and the minimum purchase level under it are features of the GIC which the parties may lawfully negotiate without intervention by the Commission.

The arguments of PG&E and CPUC concerning cost levels reflected under the price/volume commitments under the Forward Supply Service will also be rejected. As discussed above, the Commission finds that it is unnecessary to evaluate the specific cost basis for Transwestern's rates under the GIC because Southern California has alternative supply sources available—at just and reasonable rates—that effectively cap Transwestern's rates. Thus, a hearing is not required to examine issues relating to the Forward Supply Service.

Kansas Power also argues that the GIC is an unlawful attempt by Transwestern to reimpose its minimum commodity bill, which was eliminated in Opinion No. 238.[24] In Order No. 500, the Commission noted several characteristics of GICs which distinguish them from minimum bills. The Commission observed that minimum bills were not optional, were imposed only on partial requirements customers, and tended to restrain competition. In contrast, GICs (including that proposed by Transwestern) are voluntary, in that a customer can nominate any level of service, including zero volumes, without im-

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[24] 32 FERC ¶ 61,009 (1985), *reh'g denied*, Opinion No. 238-A, 36 FERC ¶ 61,175 (1986), *aff'd Transwestern Pipeline Co. v. FERC*, 820 F.2d 733 (5th Cir. 1987).

position of an exit fee, and stimulate competition by requiring the pipeline to hold its prices firm during the nomination period. Accordingly, Kansas Power's argument that Transwestern's GIC is merely a reconstituted minimum bill is rejected.

5. Reinstatement of Transwestern's PGA.

Producer Associations requests that Transwestern be permitted to reinstate its PGA on 30 days' notice, rather than be required to file under section 4 or conform to the requirements of section 154.303(b) of the regulations,[25] as required in the May 11, 1988 order. Producer Associations contends that the GIC guidelines in Order No. 500[26] only require that a pipeline maintain a price or pricing formula during the effectiveness of the GIC, not until the commencement of the next available PGA election period. Producer Associations argues that the Commission should "suspend" rather than terminate Transwestern's PGA during the effectiveness of the GIC to avoid a time lag between the end of the GIC and reinstitution of the PGA. Producer Associations contends that the requirement in the May 11, 1988 order that Transwestern file a section 4 application or comply with the PGA election procedures in section 154.303(b) may disrupt pipelines' relationships with producers and discourage implementation of GICs. It notes that the May 11, 1988 order requires Transwestern to terminate its PGA before it knows whether Southern California will nominate sufficient volumes under the GIC to make it viable.

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[25] *FERC Statutes and Regulations* ¶ 30,778 (1987), to be codified at 18 C.F.R. § 154.303(b). Under section 154.303(b)(6), a pipeline must elect to file for a PGA by December 1 of the year preceding an election period. The election procedures provide for an initial election commencing on June 1, 1988 and on January 1 of each third year thereafter.

[26] To be codified at 18 C.F.R. § 2.105.

Producer Associations' request will be denied. In accepting the GIC certificate, Transwestern is agreeing to the termination, not suspension of its PGA. In order to reinstate its PGA, Transwestern must either comply with the PGA election regulations or furnish evidence sufficient to support its position that waiver of those regulations is warranted. This requirement is unlikely to either adversely affect the business relationship between pipelines and producers or discourage implementation of GICs. In assuring pipelines a mechanism to recover costs, on a monthly basis, of maintaining long-term supplies, sufficient incentives have been provided in the GIC guidelines for pipelines to implement them and for producers to support their adoption. The requirement that a pipeline comply with the regulations to reinstate its PGA does not remove those incentives. Transwestern can limit any inconvenience in complying with the regulations by timing the termination of the PGA election period, or, alternatively, can present evidence showing that waiver of the regulation is warranted.

6. Warranty of supply.

Ordering Paragraph (B)(2) of the Commission's May 11, 1988 order required Transwestern to remove exculpatory language from its tariff concerning its gas supply obligation under the GIC and to include language therein warranting the security of such supplies except by reason of *force majeure*. Transwesern argues that the warranty condition is unnecessary because, as the Commission found in its May 11, 1988 order, it lacks market power in the southern California market and, therefore, Southern California does not need such a condition. Transwestern also complains that it does not presently have, nor can it likely obtain, a parallel commitment from its suppliers. Transwestern argues that any remedies for its failure to deliver beyond refund of the GIC charge should be negotiated by the parties. It requests that the Commission clarify whether the warranty condition was in-

tended to apply only to its GIC or extends to other sales services it provides.

Transwestern further contends that the warranty condition is unreasonable because the condition requires it to provide a service for which it will not be compensated and unlawfully exposes it to an unknown financial risk. Transwestern contends that imposition of the condition exceeds the Commission's powers under section 7 and would result in an unlawful change in its rates in violation of sections 4 and 5. Transwestern asks that the condition be deleted and in lieu thereof states its willingness to affirm that it bears a firm-service obligation concerning the GIC.

The Commission clarifies that it intended a firm-service obligation to attach to the provision of service by Transwestern under the GIC, excused only by reason of *force majeure*. By "*force majeure*" the Commission refers to acts of God, war, etc., and not mere economic infeasibility (*e.g.*, failure to obtain gas supply to obtain a "sufficient" profit for the pipeline). The Commission finds that this construction of that term is appropriate for the GIC. However, the above discussion is not intended as a general interpretation of the term as used in other contexts of services.

7. Need for market surveillance mechanism.

CPUC contends that even if market forces are sufficient to maintain rates under the GIC in a just and reasonable range at present, there is no assurance that this will be the case in the future. CPUC thus argues that a formal mechanism should be established to ensure that Transwestern's price/volume commitments under the GIC remain at or below a just and reasonable ceiling.

The Commission concludes that a formal mechanism to monitor Transwestern's charges under the GIC need not be instituted at this time. Transwestern and other pipe-

lines serving the southern California market are presently required to submit a substantial amount of data on a monthly and annual basis. The Commission will carefully analyze these data as well as other information relating to supply and demand characteristics in this market in order to monitor the operation of Transwestern's GIC. Affected parties themselves may bring to the Commission's attention evidence of supply imbalances or other conditions which hinder the operation of competitive pricing under the GIC.

8. Miscellaneous GIC issues.

Several additional issues concerning the GIC have been raised on rehearing. Kansas Power complains that the Commission has given insufficient consideration to the public interest in maintaining the presence of pipelines in the market as gas merchants. It is concerned that approval and implementation of the GIC could remove Transwestern from the market as a major gas supplier (i.e., if Southern California nominates zero volumes under the GIC). Kansas Power argues that the Commission must assess whether this potential consequence of implementation of the GIC would be anticompetitive.[27]

Kansas Power's concerns are misplaced. As noted in Order No. 500, the Commission's purpose in proposing implementation of GICs was to promote a rational, efficient pricing structure for the pipeline merchant function as the industry repositions to provide open access transportation. The evidence overwhelmingly demonstrates that the southern California market is competitive and that Transwestern's implementation of a GIC, as compared with either its provision of sales service under its CDQ Rate Schedule, or no significant firm sales service at all, would have little if any impact on the competitive structure of that market. Transwestern's sole

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[27] *Citing Connecticut Light and Power Co.*, 8 FERC ¶ 61,187, at p. 61,653 (179), *reh'g denied*, 9 FERC ¶ 61,313 (1979).

affected customer, Southern California, is a large, sophisticated participant in the market for gas sales and has multiple alternative sources to meet its needs. The Commission is concerned more directly with the preservation of competition rather than with individual competitors. If Southern California were to nominate zero volumes under Transwestern's GIC, thus effectively foreclosing Transwestern as a major firm seller of gas in southern California, it would do so for competitive, and not anti-competitive, reasons.[28] Even if Transwestern were forced out of the firm sales market, it would remain as a gas supplier under its new IS service. Further, Transwestern would remain as a transporter to the southern California market. Thus, any market impacts would be minimal.

Williams notes that the May 11, 1988 order grants Transwestern permission to abandon sales service to the extent its firm sales obligation exceeds customer nominations under the GIC. It requests that the Commission clarify "that a zero nomination in and of itself results in abandonment of the sales service involved," and that such abandonment not only relieves Transwestern of any sales obligation, but also fully relieves its customers of their corresponding purchase obligations. In addition, Williams requests the Commission to clarify that at the end of the term of the firm sales contract which is converted to firm transportation, the Commission has pre-granted the abandonment of such transportation service as to both Transwestern and its affected customer.

Transwestern's authority to abandon sales service arises as a result of the Commission's approval of the application for pre-granted abandonment authority. The cir-

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[28] In a competitive environment, purchasers frequently diversify their supply requirements to strengthen upstream competition. There is no reason to assume, given competitive pricing by Transwestern, that Southern California would not likewise act to diversify further its supply portfolio.

cumstance which causes that authority to become effective is a customer's nomination under the GIC of a volume less than its firm sales entitlement. While the customer's nomination serves as a triggering mechanism for the abandonment, the authority to abandon stems from the Commission's pre-granted approval of Transwestern's application. Williams correctly notes that abandonment of Transwestern's sales obligation necessarily terminates its purchase obligation. A customer cannot purchase gas Transwestern is not authorized to sell. Finally, Williams correctly observes that upon termination of any sales contract which has been converted to firm transportation, abandonment-of-transportation service is authorized upon the expiration of that contract.[29]

Transwestern seeks clarification of the Commission's statement in the May 11, 1988 order that future revisions of the GIC require certificate authority. It argues that inasmuch as the Commission has provided pre-granted abandonment authority for it to abandon firm sales in excess of its customers' GIC nominations, future revisions of the GIC should involve rate changes under section 4 rather than section 7.

The Commission clarifies that the type of authority (i.e., section 4 or section 7) needed for revision of the GIC depends on the nature of the revision sought. Transwestern is correct that changes in the level of rates will be considered under section 4. However, substantial changes in the manner in which the GIC operates or in its basic structure must be reviewed and approved under section 7 before they can be put into effect.[30]

Transwestern notes that the Order No. 500 series is not final. It requests clarification that if it accepts its GIC certificate, it may do so without prejudicing its

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[29] *See* 18 C.F.R. § 284.221(d) (1987).

[30] *See, e.g., Reynolds Metals Co. v. FPC,* 534 F.2d 379 (D.C. Cir. 1976).

rights with respect to the final outcome of Order No. 500.

The Commission is unclear as to the precise import of Transwestern's request for clarification. To the extent that future refinements of the policies established in Order No. 500 affect Transwestern's GIC, the Commission will take into consideration Transwestern's reliance on current policy.[31]

Finally, on June 10, 1988 Transwestern filed a motion, pursuant to Rule 2008 of the Commission's Rules of Practice and Procedure,[32] requesting that the Commission modify Ordering Paragraph (B)(7) the May 11, 1988 order, which had waived application of section 157.20(a) of the regulations,[33] and required Transwestern to accept or reject its GIC certificate within 45 days. By order,[34] issued June 27, 1988, the Commission granted Transwestern an extension until 30 days after issuance of its order on rehearing of the May 11, 1988 order, and indicated that it would consider therein whether a further extension was warranted. The Commission will grant, in part, Transwestern's request for a stay until December 31, 1988. That deadline is the same one that Transwestern, as well as all jurisdictional natural gas pipelines, must file to recover, through a fixed charge, take-or-pay buy-out and buy-down costs. See 18 C.F.R. § 2.104(c) (1987).

B. Interruptible Sales Service.

1. Minimum rate.

In its May 11, 1988 order, the Commission set the maximum rate for the new IS service equal to the 100

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[31] *See, e.g., City of Chicago v. FPC*, 385 F.2d 629, 637 (D.C. Cir. 1967); and *Chevron Oil Co. v. Hason*, 404 U.S. 97 (1971).

[32] 18 C.F.R. § 385.2008 (1987).

[33] 18 C.F.R. § 157.20(a) (1987).

[34] 43 FERC ¶ 61,549 (1988).

percent load factor rate for Transwestern's CDQ-1 rate schedule and the minimum rate equal to the WACOG plus variable costs included in Transwestern's small customer SG rate schedule. The Commission also imposed a condition requiring Transwestern to treat sales under the new IS rate schedule the same as any other interruptible sales or transportation service for the purpose of scheduling, allocating capacity or curtailing service.

Producer Associations contends that the noted condition forecloses the possibility of preference and cross-subsidization and requests the Commission to remove the floor rate requirement from the IS service. It argues that Transwestern should be free to set its price for its IS sales, subject to the constraint that if the sale fails to return variable costs, Transwestern's shareholders should absorb the shortfall. Transwestern argues that the Commission should reduce the floor for the IS service to reflect the lower of its PGA WACOG or the lowest interruptible sales rate on its system. ANR contends that the floor rate for the IS service is contrary to the Commission's purported policy of requiring interruptible services to absorb a portion of Transwestern's fixed costs. It argues that Transwestern's interruptible customers use the latter's facilities and should therefore bear part of Transwestern's capacity-related cost.[35]

The Commission adheres to its position in the prior order that the minimum rate for the IS service reflect average gas costs and other variable cost components of Transwestern's small customer rates. Producer Associations's proposal for a marginal cost floor price increases the potential for improper cross-subsidization and preference without providing sufficient incentives to increase sales. On the other hand, ANR's proposal that the IS floor rate provide for recovery of some portion of fixed

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[35] *Citing Natural Gas Pipeline Company of America*, 39 FERC ¶ 61,153, at p. 61,606 (1987).

costs unnecessarily circumscribes its effectiveness as a marketing tool. Unless all IS sales are made at the minimum IS rate, the program will necessarily contribute to recovery of Transwestern's fixed costs. Accordingly, ANR's position is rejected.

2. Affiliate reporting requirements.

Transwestern objects to the affiliate reporting requirements respecting the IS service imposed in the May 11, 1988 order, arguing that the requirements are unnecessarily burdensome, unduly discriminatory and inconsistent with other Commission policies.[36]

In *Northern Natural*, footnote 36, *supra*, the Commission carefully considered a number of objections to prior notice requirements for affiliate sales identical to these at issue here. The Commission determined that the affiliate reporting requirements represented a reasonable balancing of the divergent interests of the parties concerned in that the pipeline's interruptible sales program provided it with a significant degree of flexibility in matching purchases and sales, but also resulted in a potential to discriminate and to shield affiliates from competitive forces contrary to Commission policy. The Commission concluded that the moderate 30-day delay in affiliate sales transactions engendered by the reporting requirements provided the Commission and other parties the time necessary to review a transaction and evaluate its potential for undue discrimination. The Commission's reasoning in *Northern Natural* is equally applicable here, and Transwestern's request for elimination of the affiliate reporting requirements will be denied.

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[36] Transwestern appends a copy of the request for rehearing filed on April 19, 1988 by Northern Natural Gas Company (Northern Natural) of the Commission's March 11, 1988 order [42 FERC ¶ 61,303 (1988)] which also addressed this issue. By order issued June 23, 1988 [43 FERC ¶ 61,515 (1988)], the Commission denied Northern Natural's rehearing request.

3. Availability of take-or-pay credits.

ANR requests the Commission to clarify that take-or-pay credits are available for its transportation of gas sold under Transwestern's new IS service. It contends that unless credits are received, it would be adversely affected, inasmuch as credits are available for the transportation of gas sold directly by producers. Without the availability of credits, ANR asserts that its take-or-pay problems will be exacerbated as former customers switch to Transwestern's IS service. Transwestern, in contrast, argues that credits should not be available.[37]

As noted in *Northern Natural*, the take-or-pay crediting requirements in Order No. 500 are intended to cover gas transported through open-access pipeline, regardless of whether the gas is purchased directly from a producer or from a secondary purchaser. Accordingly, the request for clarification of ANR is granted and that of Transwestern is denied.

4. Impact of IS service on competitors.

ANR argues that approval of Transwestern's IS service will ameliorate Transwestern's take-or-pay problems by exacerbating those of other pipelines by displacing their sales rather than increasing the market for natural gas. This argument is virtually identical to that raised by ANR in *Northern Natural*, *supra*, and will likewise be rejected here. The Commission will not exercise its regulatory mandate to shield pipelines from competition. Rather, pipelines must adjust to changing market conditions to protect sales and limit their respective take-or-pay exposure. ANR itself may institute an interruptible sales program. The Commission will not deprive Transwestern and its customers of the benefits of its IS service

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[37] Transwestern incorporates by reference the arguments raised on rehearing by Northern Natural Gas Company in its April 19, 1988 request for rehearing. *See* footnote 36, *supra*.

to protect ANR's sales base from potential erosion by Transwestern's IS sales.

The Commission orders:

(A) The requests for rehearing of Southern California, CPUC and ANR are granted to the extent indicated in the above. In all other respects, the other requests for rehearing are denied.

(B) The requests for clarification of Southern California, CPUC, Williams and Transwestern are granted as set forth in the text above. In all other respects, the requests for clarification are denied.

(C) The June 10, 1988 request by Transwestern for an extension of time to accept or reject the GIC is granted in part, until December 31, 1988.

STATUTES INVOLVED

NATURAL GAS ACT

Rates and Charges

Sec. 4. (a) All rates and charges made, demanded, or received by any natural-gas company for or in connection with the transportation or sale of natural gas subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges, shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

(b) No natural-gas company shall, with respect to any transportation or sale of natural gas subject to the jurisdiction of the Commission, (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

(c) Under such rules and regulations as the Commission may prescribe, every natural-gas company shall file with the Commission, within such time (not less than sixty days from the date this act takes effect) and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection, schedules showing all rates and charges for any transportation or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

(d) Unless the Commission otherwise orders, no change shall be made by any natural-gas company in any such rate, charge, classification, or service, or in any rule,

regulations, or contract relating thereto, except after thirty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the thirty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Whenever any such new schedule is filed the Commission shall have authority, either upon complaint of any State, municipality, State commission, or gas distributing company or upon its own initiative without complaint, at once, and if it so orders, without answer or formal pleading by the natural-gas company, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the natural-gas company affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect; and after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of the suspension period, on motion of the natural-gas company making the filing, the proposed change of rate, charge, classification, or service shall go into effect. Where increased rates or

charges are thus made effective, the Commission may, by order, require the natural-gas company to furnish a bond, to be approved by the Commission, to refund any amounts ordered by the Commission, to keep accurate accounts in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts were paid, and, upon completion of the hearing and decision, to order such natural-gas company to refund, with interest, the portion of such increased rates or charges by its decision found not justified. At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the natural-gas company, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible.

Fixing Rates and Charges; Determination of Cost of Production or Transportation

Sec. 5. (a) Whenever the Commission, after a hearing had upon its own motion or upon complaint of any State, municipality, State commission, or gas distributing company, shall find that any rate, charge, or classification demanded, observed, charged, or collected by any natural-gas company in connection with any transportation or sale of natural gas, subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory, or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order: *Provided, however*, That the Commission shall have no power to order any increase in any rate contained in the currently effective schedule of such natural-gas company on file with the Commission, unless such increase is in accordance with a new schedule

filed by such natural-gas company; but the Commission may order a decrease where existing rates are unjust, unduly discriminatory, preferential, otherwise unlawful, or are not the lowest reasonable rates.

(b) The Commission upon its own motion, or upon the request of any State commission, whenever it can do so without prejudice to the efficient and proper conduct of its affairs, may investigate and determine the cost of the production or transportation of natural gas by a natural-gas company in cases where the Commission has no authority to establish a rate governing the transportation or sale of such natural gas.

Extension of Facilities; Abandonment of Service

Sec. 7. (a) Whenever the Commission, after notice and opportunity for hearing, finds such action necessary or desirable in the public interest, it may by order direct a natural-gas company to extend or improve its transportation facilities, to establish physical connection of its transportation facilities with the facilities of, and sell natural gas to, any person or municipality engaged or legally authorized to engage in the local distribution of natural or artificial gas to the public, and for such purpose to extend its transportation facilities to communities immediately adjacent to such facilities or to territory served by such natural-gas company, if the Commission finds that no undue burden will be placed upon such natural-gas company thereby: *Provided*, That the Commission shall have no authority to compel the enlargement of transportation facilities for such purposes, or to compel such natural-gas company to establish physical connection or sell natural gas when to do so would impair its ability to render adequate service to its customers.

(b) No natural-gas company shall abandon all or any portion of its facilities subject to the jurisdiction of the Commission, or any service rendered by means of such facilities, without the permission and approval of the

Commission first had and obtained after due hearing, and a finding by the Commission that the available supply of natural gas is depleted to the extent that the continuance of service is unwarranted, or that the present or future public convenience or necessity permit such abanonment.

(c) (1) (A) No natural-gas company or person which will be a natural-gas company upon completion of any proposed construction or extension shall engage in the transportation or sale of natural gas, subject to the jurisdiction of the Commission, or undertake the construction or extension of any facilities therefor, or acquire or operate any such facilities or extensions thereof, unless there is in force with respect to such natural-gas company a certificate of public convenience and necessity issued by the Commission authorizing such acts or operations: *Provided, however*, That if any such natural-gas company or predecessor in interest was bona fide engaged in transportation or sale of natural gas, subject to the jurisdiction of the Commission, on the effective date of this amendatory Act, over the route or routes or within the area for which application is made and has so operated since that time, the Commission shall issue such certificate without requiring further proof that public convenience and necessity will be served by such operation, and without further proceedings, if application for such certificate is made to the Commission within ninety days after the effective date of this amendatory Act. Pending the determination of any such application, the continuance of such operation shall be lawful.

(B) In all other cases the Commission shall set the matter for hearing and shall give such reasonable notice of the hearing thereon to all interested persons as in its judgment may be necessary under rules and regulations to be prescribed by the Commission; and the application shall be decided in accordance with the procedure provided in subsection (e) of this section and such certifi-

cate shall be issued or denied accordingly: *Provided, however,* That the Commission may issue a temporary certificate in cases of emergency, to assure maintenance of adequate service or to serve particular customers, without notice or hearing, pending the determination of an application for a certificate, and may by regulation exempt from the requirements of this section temporary acts or operations for which the issuance of a certificate will not be required in the public interest.

(2) The Commission may issue a certificate of public convenience and necessity to a natural-gas company for the transportation in interstate commerce of natural gas used by any person for one or more high-priority uses, as defined, by rule, by the Commission, in the case of—

(A) natural gas sold by the producer to such person; and

(B) natural gas produced by such person.

(d) Application for certificates shall be made in writing to the Commission, be verified under oath, and shall be in such form, contain such information, and notice thereof shall be served upon such interested parties and in such manner as the Commission shall, by regulation, require.

(e) Except in the cases governed by the provisos contained in subsection (c)(1) of this section, a certificate shall be issued to any qualified applicant therefor, authorizing the whole or any part of the operation, sale, service, construction, extension, or acquisition covered by the application, if it is found that the applicant is able and willing properly to do the acts and to perform the service proposed and to conform to the provisions of the Act and the requirements, rules, and regulations of the Commission thereunder, and that the proposed service, sale, operation, construction, extension, or acquisition, to the extent authorized by the certificate, is or will be required by the present or future public convenience and

necessity; otherwise such application shall be denied. The Commission shall have the power to attach to the issuance of the certificate and to the exercise of the rights granted thereunder such reasonable terms and conditions as the public convenience and necessity may require.

(f) (1) The Commission, after a hearing had upon its own motion or upon application, may determine the service area to which each authorization under this section is to be limited. Within such service area as determined by the Commission a natural-gas company may enlarge or extend its facilities for the purpose of supplying increased market demands in such service area without further authorization; and

(2) If the Commission has determined a service area pursuant to this subsection, transportation to ultimate consumers in such service area by the holder of such service area determination, even if across State lines, shall be subject to the exclusive jurisdiction of the State commission in the State in which the gas is consumed. This section shall not apply to the transportation of natural gas to another natural gas company.

(g) Nothing contained in this section shall be construed as a limitation upon the power of the Commission to grant certificates of public convenience and necessity for service of an area already being served by another natural-gas company.

(h) When any holder of a certificate of public convenience and necessity cannot acquire by contract, or is unable to agree with the owner of property to the compensation to be paid for, the necessary right-of-way to construct, operate, and maintain a pipe line or pipe lines for the transportation of natural gas, and the necessary land or other property, in addition to right-of-way, for the location of compressor stations, pressure apparatus, or other stations or equipment necessary to the proper operation of such pipe line or pipe lines, it may acquire

the same by the exercise of the right of eminent domain in the district court of the United States for the district in which such property may be located, or in the State courts. The practice and procedure in any action or proceeding for that purpose in the district court of the United States shall conform as nearly as may be with the practice and procedure in similar action or proceeding in the courts of the State where the property is situated: *Provided,* That the United States district courts shall only have jurisdiction of cases when the amount claimed by the owner of the property to be condemned exceeds $3,000.

NATURAL GAS POLICY ACT

SEC. 601. COORDINATION WITH THE NATURAL GAS ACT.

(a) JURISDICTION OF THE COMMISSION UNDER THE NATURAL GAS ACT.—

(1) SALES.—

(A) NATURAL GAS NOT COMMITTED OR DEDICATED. For purposes of section 1(b) of the Natural Gas Act, effective on the first day of the first month beginning after the date of the enactment of this Act, the provisions of the Natural Gas Act and the jurisdiction of the Commission under such Act shall not apply to natural gas which was not committed or dedicated to interstate commerce as of the day before the date of enactment of this Act solely by reason of any first sale of such natural gas.

(B) COMMITTED OR DEDICATED NATURAL GAS.— Effective beginning on the first day of the first month beginning after the date of the enactment of this Act, for purposes of section 1(b) of the Natural Gas Act, the provisions of such Act and the jurisdiction of the Commission under such Act shall not apply solely by reason of any first sale of natural gas which is committed or dedicated to interstate commerce as of the day before the date of the enactment of this Act and which is—

(i) high-cost natural gas (as defined in section 107(c)(1),(2),(3), or (4) of this Act);

(ii) new natural gas (as defined in section 102(c) of this Act); or

(iii) natural gas produced from any new, onshore production well (as defined in section 103(c) of this Act).

(C) AUTHORIZED SALES OR ASSIGNMENTS.—For purposes of section 1(b) of the Natural Gas Act, the provisions of the Natural Gas Act and the jurisdiction of the Commission under such Act shall not apply by reason of any sale of natural gas—

(i) authorized under section 302(a) or 311(b); or

(ii) pursuant to any assigned authorized under section 312(a).

(D) NATURAL-GAS COMPANY.—For purposes of the Natural Gas Act, the term "natural-gas company" (as defined in section 2(6) of such Act) shall not include any person by reason of, or with respect to, any sale of natural gas if the provisions of the Natural Gas Act and the jurisdiction of the Commission do not apply to such sale solely by reason of subparagraph (A), (B), or (C) of this paragraph.

(E) CERTAIN ADDITIONAL NATURAL GAS.—For purposes of section 1(b) of the Natural Gas Act, the provisions of the Natural Gas Act and the jurisdiction of the Commission under such Act shall not apply solely by reason of any first sale of natural gas which is committed or dedicated to interstate commerce as of the day before the date of the enactment of this Act and which is not subject to a maximum lawful price under subtitle A of title I by reason of section 121(f), effective as of the date such gas ceases to be subject to such maximum lawful price.

(2) TRANSPORTATION.—

(A) JURISDICTION OF THE COMMISSION.—For purposes of section 1(b) of the Natural Gas Act the provisions of such Act and the jurisdiction of the Commission under such Act shall not apply to any transportation in interstate commerce of natural gas if such transportation is—

(i) pursuant to any order under section 302 (c) or section 303(b), (c), (d), or (h) of this Act; or

(ii) authorized by the Commission under section 311(a) of this Act.

(B) NATURAL-GAS COMPANY.—For purposes of the Natural Gas Act, the term "natural-gas company" (as defined in section 2(6) of such Act) shall not include any person by reason of, or with respect to, any transportation of natural gas if the provisions of the Natural Gas Act and the jurisdiction of the Commission under the Natural Gas Act do not apply to such transportation by reason of subparagraph (A) of this paragraph.

(b) CHARGES DEEMED JUST AND REASONABLE.—

(1) SALES.—

(A) FIRST SALES.—Subject to paragraph (4), for purposes of sections 4 and 5 of the Natural Gas Act, any amount paid in any first sale of natural gas shall be deemed to be just and reasonable if—

(i) such amount does not exceed the applicable maximum lawful price established under title I of this Act; or

(ii) there is no applicable maximum lawful price solely by reason of the elimination of price controls pursuant to subtitle B of title I of this Act.

(B) EMERGENCY SALES.—For purposes of sections 4 and 5 of the Natural Gas Act, any amount paid in any sale authorized under section 302(a) shall be deemed to be just and reasonable if such amount does not exceed the fair and equitable price established under such section and applicable to such sale.

(C) SALES BY INTRASTATE PIPELINES.—For purposes of sections 4 and 5 of the Natural Gas Act, any amount paid in any sale authorized by the Commission under section 311(b) shall be deemed to be just and reasonable if such amount does not exceed the fair and equitable price established by the Commission and applicable to such sale.

(D) ASSIGNMENTS.—For purposes of sections 4 and 5 of the Natural Gas Act, any amount paid pursuant to the terms of any contract with respect to that portion of which the Commission has authorized an assignment authorized under section 312(a) shall be deemed to be just and reasonable if such amount does not exceed the applicable maximum lawful price established under title I of this Act.

(E) AFFILIATED ENTITIES LIMITATION.—For purposes of paragraph (1), in the case of any first sale between any interstate pipeline and any affiliate of such pipeline any amount paid in any first sale shall be deemed to be just and reasonable if, in addition to satisfying the requirements of such paragraph, such amount does not exceed the amount paid in comparable first sales between persons not affiliated with such interstate pipeline.

(2) OTHER CHARGES.—

(A) ALLOCATION.—For purposes of sections 4 and 5 of the Natural Gas Act, any amount paid by any interstate pipeline for transportation, storage, delivery or other services provided pursuant to any order under section 303(b), (c), or (d) of this Act shall be deemed to be just and reasonable if such amount is prescribed by the President under section 303(h)(1).

(B) TRANSPORTATION.—For purposes of sections 4 and 5 of the Natural Gas Act, any amount paid by

any interstate pipeline for any transportation authorized by the Commission under section 311(a) of this Act shall be deemed to be just and reasonable if such amount does not exceed that approved by the Commission under such section.

(c) GUARANTEED PASSTHROUGH.—

(1) CERTIFICATE MAY NOT BE DENIED BASED UPON PRICE.—The Commission may not deny, or condition the grant of, any certificate under section 7 of the Natural Gas Act based upon the amount paid in any sale of natural gas, if such amount is deemed to be just and reasonable under subsection (b) of this section.

(2) RECOVERY OF JUST AND REASONABLE PRICES PAID.—For purposes of sections 4 and 5 of the Natural Gas Act, the Commission may not deny any interstate pipeline recovery of any amount paid with respect to any purchase of natural gas if, under subsection (b) of this section, such amount is deemed to be just and reasonable for purposes of sections 4 and 5 of such Act, except to the extent the Commission determines that the amount paid was excessive due to fraud, abuse, or similar grounds.

Nos. 90-344, 90-367

Supreme Court, U.S.
FILED
OCT 9 1990
JOSEPH F. SPANIOL, JR.
CLERK

In The

Supreme Court of the United States

October Term, 1990

TRANSWESTERN PIPELINE COMPANY,

Petitioner,

v.

KANSAS POWER AND LIGHT COMPANY, *et al.*,

Respondents.

FEDERAL ENERGY REGULATORY COMMISSION,

Petitioner,

v.

PUBLIC UTILITIES COMMISSION OF CALIFORNIA, *et al.*,

Respondents.

On Petitions For A Writ Of Certiorari To The United States Court Of Appeals For The District Of Columbia Circuit

BRIEF IN OPPOSITION OF RESPONDENTS, THE KANSAS POWER AND LIGHT COMPANY AND THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

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QUESTION PRESENTED

Whether the court of appeals erred in determining that the filed rate doctrine under the Natural Gas Act did not allow the Federal Energy Regulatory Commission to authorize Transwestern Pipeline Company to retroactively increase its rates for gas already sold to its customers.

PARTIES TO THE PROCEEDING

In addition to Respondents, The Kansas Power and Light Company and the Public Utilities Commission of the State of California, the parties to the proceeding before the court of appeals were:

Citizens Energy Corporation
El Paso Natural Gas Company
Federal Energy Regulatory Commission
Natural Gas Clearinghouse Inc.
Pacific Gas and Electric Company
Process Gas Consumers Group
PSI, Inc.
Southern California Gas Company
Southwest Gas Corporation
Texas Eastern Transmission Corporation
Transwestern Pipeline Company
Williams Natural Gas Company

RESPONDENT'S RULE 29.1 STATEMENT

The Kansas Power and Light Company is a publicly traded corporation. It has no parent company and no subsidiaries which are not wholly owned.

TABLE OF CONTENTS

Page

QUESTION PRESENTED i

PARTIES TO THE PROCEEDING ii

RESPONDENT'S RULE 29.1 STATEMENT iii

TABLE OF CONTENTS iv

TABLE OF AUTHORITIES v

STATEMENT OF THE CASE 2

ARGUMENT 4

I. THIS COURT SHOULD NOT HOLD THIS CASE SUBJECT TO ITS RULING IN THE *AGD II* APPEAL 5

II. THE COURT OF APPEALS FOLLOWED AND APPLIED ESTABLISHED PRINCIPLES OF STATUTORY CONSTRUCTION 6

A. The Statutory Framework and the Filed Rate Doctrine 6

B. The Court of Appeals Properly Employed the Applicable Principles of Statutory Construction 10

1. The Filed Rate Doctrine 11

2. Waiver of the Filed Rate Doctrine 13

III. THE COURT OF APPEALS' RULING DOES NOT CONFLICT WITH THE NGPA OR PGA REGULATIONS 16

IV. THE COURT OF APPEALS' OPINION IS NOT IN CONFLICT WITH RULINGS BY OTHER FEDERAL COURTS OF APPEALS 19

CONCLUSION 22

TABLE OF AUTHORITIES

Page

CASES

Arkansas Louisiana Gas Co. v. Hall, 453 U.S. 571 (1981) ..... *passim*

Associated Gas Distributors v. FERC, 893 F.2d 349 (D.C. Cir. 1989) 5

California v. FERC, 109 S. Ct. 2024 (1990) 11

Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837 (1984) 10, 11

City of Girard v. FERC, 790 F.2d 919 (D.C. Cir. 1986) 13

City of Piqua v. FERC, 610 F.2d 950 (D.C. Cir. 1979) ..8, 13

Columbia Gas Transmission Corp. v. FERC, 831 F.2d 1135 (D.C. Cir. 1987) 10

FERC v. Martin Exploration Management Company, 486 U.S. 204 (1988) 18

FPC v. Hope Natural Gas Co., 320 U.S. 591 (1941) 14

FPC v. Natural Gas Pipeline Co., 315 U.S. 575 (1942) 18

Hall v. FERC, 691 F.2d 1184 (5th Cir. 1982) 13

Louisville & Nashville R. Co. v. Maxwell, 237 U.S. 94 (1915) 9, 14

Lowden v. Simonds-Shield-Lonsdale Grain Co., 306 U.S. 516 (1939) 8

Maislin Industries, U.S., Inc. v. Primary Steel, Inc., 110 S. Ct. 2759 (1990) ..... *passim*

Market Street Ry. v. Railroad Comm'n, 324 U.S. 548 (1945) 18

Maryland People's Counsel v. FERC, 761 F.2d 780 (D.C. Cir. 1985) 14

TABLE OF AUTHORITIES – Continued

Page

Montana-Dakota Utilities Company v. Northwestern Public Service Company, 341 U.S. 246 (1951) 7

Pennsylvania R. Co. v. International Coal Co., 230 U.S. 184 (1913) 8

Phillips Petroleum Co. v. FERC, 902 F.2d 795 (10th Cir. 1990) 19, 21

Square D Co. v. Niagara Frontier Traffic Bureau, Inc., 476 U.S. 409 (1986) 16

Texas Eastern Transmission Corp. v. FERC, 769 F.2d 1053 (5th Cir. 1985) 19, 20, 21

Transwestern Pipeline Co. v. FERC, 897 F.2d 570 (D.C. Cir. 1990) 10, 12

STATUTES

Natural Gas Act

§4(a), 15 U.S.C. §717c(a) 7, 14

§4(b), 15 U.S.C. §717c(b) 15

§4(c), 15 U.S.C. §717c(c) 7, 15

§4(d), 15 U.S.C. §717c(d) 7, 13

Natural Gas Policy Act of 1978

§1(21)(A), 15 U.S.C. §3301(21)(A) 19

§1(21)(B), 15 U.S.C. §3301(21)(B) 19

§110(a)(2), 15 U.S.C. §3320(a)(2) 19

§601, 15 U.S.C. §3431 16

ADMINISTRATIVE DECISIONS

Kentucky West Virginia Gas Co., 37 FERC ¶61,310 (1986) 21

TABLE OF AUTHORITIES – Continued

Page

NITL – Petition to Institute Rulemaking on Negotiated Motor Common Carrier Rates, 3 I.C.C.2d 99 (1986) 9

NITL – Petition to Institute Rulemaking on Negotiated Motor Common Carrier Rates, 5 I.C.C.2d 623 (1989) 9

Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol, Order No. 500, FERC Stats. & Regs. ¶ 30,761, *modified*, Order No. 500-A, FERC Stats. & Regs. ¶ 30,770, *reh'g granted in part*, Order No. 500-B, FERC Stats. & Regs. ¶ 30,772, *modified*, Order No. 500-C, FERC Stats. & Regs. ¶ 30,786 (1987), *modified*, Order No. 500-D, FERC Stats. & Regs. ¶ 30,800, *reh'g denied*, Order No. 500-E, 43 FERC ¶ 61,234, *modified*, Order No. 500-F, FERC Stats. & Regs. ¶ 30,841 (1988), *reh'g denied*, Order No. 500-G, 46 FERC ¶ 61,148 (1989), *remanded sub nom. American Gas Ass'n v. FERC*, 888 F.2d 136 (D.C. Cir. 1989), *order on remand*, Order No. 500-H, FERC Stats. & Regs. ¶ 30,867 (1989), *reh'g denied in part*, Order No. 500-I, FERC Stats. & Regs. ¶ 30,880 (1990), *remanded sub nom. American Gas Ass'n v. FERC*, No. 87-1588, *et al.*, (D.C. Cir. Aug. 20, 1990) 3

Tennessee Pipeline Co., 33 FERC ¶ 61,014 (1985) 17

Tennessee Pipeline Co., 33 FERC ¶ 61,061 (1985) 17

Texas Eastern Transmission Corp., 44 FERC ¶61,413 (1988) 17

Transwestern Pipeline Co., 40 FERC ¶61,324 (1987) 17

REGULATIONS

18 C.F.R. §154.305(c)(3) 3

Nos. 90-344, 90-367

In The

Supreme Court of the United States

October Term, 1990

TRANSWESTERN PIPELINE COMPANY,

Petitioner,

v.

KANSAS POWER AND LIGHT COMPANY, *et al.*,

Respondents.

FEDERAL ENERGY REGULATORY COMMISSION,

Petitioner,

v.

PUBLIC UTILITIES COMMISSION OF CALIFORNIA, *et al.*,

Respondents.

On Petitions For A Writ Of Certiorari To The United States Court Of Appeals For The District Of Columbia Circuit

BRIEF IN OPPOSITION OF RESPONDENTS, THE KANSAS POWER AND LIGHT COMPANY AND THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

STATEMENT OF THE CASE

The Respondent, The Kansas Power and Light Company (KPL), is a natural gas local distribution company doing business in the states of Kansas, Missouri, and Oklahoma. It is a customer of the Williams Natural Gas Company (WNG) which ceased being a customer of Petitioner, Transwestern Pipeline Company (Transwestern) on February 1, 1988. The Respondent, Public Utilities Commission of the State of California (CPUC), is a state agency which regulates Southern California Gas Company (SoCal), which had previously been a sales customer of Transwestern. The CPUC represents the interests of natural gas consumers throughout California in administrative and judicial proceedings. Under the rulings of the Federal Energy Regulatory Commission, reviewed below by the United States Court of Appeals for the District of Columbia, Transwestern was authorized to direct bill certain costs to WNG, which in turn was allowed to recover them from KPL, and to SoCal, which would seek to recover them from southern California consumers, who are represented herein by the CPUC.

Petitioners challenge a decision of the court of appeals finding that a procedure proposed by Transwestern and approved by the Federal Energy Regulatory Commission (FERC or Commission) for "direct billing" of certain deferred gas costs to its customers violated the filed rate doctrine under the Natural Gas Act (NGA). Without direct billing, the pipeline would have sought to recover these costs *prospectively* as part of its sales commodity rate to its customers. Under the method approved by the Commission, however, the pipeline was authorized to assign responsibility and bill its customers for

the costs *retroactively* based on each customer's pro rata share of total contract demand on the system at an earlier time.

Transwestern proposed direct billing as part of its voluntary application for authority to implement a gas inventory charge (GIC) pursuant to guidelines established by the FERC in its Order No. 500.[1] Transwestern indicated that if the GIC was made effective, the pipeline would terminate its purchased gas adjustment clause (PGA). The PGA is the mechanism used by most pipelines to recover their cost of purchased gas. It is comprised of two components – a rate meant to reflect the cost of current gas purchases and a surcharge intended to recoup the difference between costs incurred and costs recovered.

The difference between cost recovery and cost incurrence is accrued to Account 191 – Unrecovered Purchased Gas Costs. Under currently effective regulations, a surcharge is determined annually by dividing the amount in Account 191 by the pipeline's estimate of sales for the next twelve months. 18 C.F.R. §154.305(c)(3). Over time,

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[1] *Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol*, Order No. 500, FERC Stats. & Regs. ¶ 30,761, *modified*, Order No. 500-A, FERC Stats. & Regs. ¶ 30,770, *reh'g granted in part*, Order No. 500-B, FERC Stats. & Regs. ¶ 30,772, *modified*, Order No. 500-C, FERC Stats. & Regs. ¶ 30,786 (1987), *modified*, Order No. 500-D, FERC Stats. & Regs. ¶ 30,800, *reh'g denied*, Order No. 500-E, 43 FERC ¶ 61,234, *modified*, Order No. 500-F, FERC Stats. & Regs. ¶ 30,841 (1988), *reh'g denied*, Order No. 500-G, 46 FERC ¶ 61,148 (1989), *remanded sub nom. American Gas Ass'n v. FERC*, 888 F.2d 136 (D.C. Cir. 1989), *order on remand*, Order No. 500-H, FERC Stats. & Regs. ¶ 30,867 (1989), *reh'g denied in part*, Order No. 500-I, FERC Stats. & Regs. ¶ 30,880 (1990), *remanded sub nom. American Gas Ass'n v. FERC*, No. 87-1588, *et al.*, (D.C. Cir. Aug. 20, 1990).

assuming that the pipeline is able to keep its gas marketable, the surcharge will allow the pipeline to match its revenue to its gas costs. Since, if its proposal was accepted, Transwestern would no longer have a PGA surcharge in effect, the pipeline proposed to clear its Account No. 191 by direct billing the amounts in it to its sales customers.

ARGUMENT

Review by this Court is not warranted. The ruling of the court of appeals is correct. It is consistent with basic principles of statutory construction and interpretations of the NGA and the "filed rate doctrine" by this Court. The court of appeals acted properly in barring the attempt by the pipeline and the Commission to impose retroactive charges upon consumers of natural gas. The decision below is also consistent with established principles of ratemaking for regulated utilities and with the consumer protection purposes of the NGA.

This case presents no substantial question for review by this Court. In fact, the court of appeals' ruling below is entirely consistent with the decision of this Court on the filed rate doctrine in its most recent term in *Maislin Industries, U.S., Inc. v. Primary Steel, Inc.*, 110 S. Ct. 2759 (1990). The decision of the court of appeals is also consistent with both its prior rulings and those of other courts of appeals on the same matter.

The petition for writ of certiorari should be denied.

I. THIS COURT SHOULD NOT HOLD THIS CASE SUBJECT TO ITS RULING IN THE *AGD II* APPEAL.

The Commission requests that if the Court grants its certiorari petition in *Associated Gas Distributors v. FERC* (*AGD II*), 893 F.2d 349 (D.C. Cir. 1989),[2] that it hold this case for disposition as appropriate in light of the ruling in that appeal. The Commission states that a decision in that case would "shed considerable light on the appropriate disposition of this case . . . . " Petition for Writ of Certiorari of the Federal Energy Regulatory Commission (FERC Pet.), at 11. In *AGD II*, the court of appeals rejected the use of an allocation formula for direct billing as the basis for recovery by pipelines of a portion of their current costs incurred in settling take-or-pay disputes. Even if review by this Court were appropriate in *AGD II*, the procedure urged by the Commission should not be followed in this case.

The approach proposed by the Commission would only be appropriate if it were clear that a ruling by this Court in *AGD II* would be directly applicable to this matter. In fact, the Commission's statements in its *AGD II* certiorari petition (*AGD II* Pet.) indicate that is not the situation. The Commission views its actions which are the subject of review in *AGD II* quite differently from those at issue here. In its *AGD II* petition, the Commission argued that the allocation method it had approved did not impose a rate increase for gas already sold. *AGD II* Pet., at 21-22. The Commission argued that it had

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[2] The Commission's certiorari petition was docketed in this Court as *Federal Energy Regulatory Commission v. Associated Gas Distributors, et al.*, No. 89-2016.

> instead ordered customers to pay a new rate on a prospective basis to cover a portion of the costs of [the pipeline]'s settlement of its take-or-pay exposure, and it allocated those current costs among [the pipeline]'s customers on the basis of the relative amounts of gas they did *not* purchase during the deficiency period.

Ibid. at 22. (Underscore added; italics original.) By contrast, there is no question that the present case relates to *retroactive* recovery of *past* costs and that the costs in question relate to the "gas that [Transwestern] purchased and *sold* to its customers, SoCal and Williams, prior to May 11, 1988." FERC Pet., at 9. (Emphasis added.)

In view of the above, a mere comparison of the FERC's two positions before this Court (i.e., *compare AGD II* Pet. at 21-22 *with* FERC Pet. at 9) shows that the two cases are totally different and that the present case is not certworthy.

II. THE COURT OF APPEALS FOLLOWED AND APPLIED ESTABLISHED PRINCIPLES OF STATUTORY CONSTRUCTION.

A. The Statutory Framework and the Filed Rate Doctrine.

Section 4(a) of the NGA provides that:

> [a]ll rates and charges made, demanded, or received by any natural-gas company for or in connection with the transportation or sale of natural gas subject to the jurisdiction of the Commission . . . shall be just and reasonable, and any such rate or charge that is not just and reasonable is declared to be unlawful.

15 U.S.C. §717c(a). In order to assure that rates charged by companies within the Commission's NGA jurisdiction are "just and reasonable," the Act requires that pipeline rates be filed with the Commission and kept available for public inspection, 15 U.S.C. §717c(c), and prohibits the granting of "undue preference or advantage" to any customer or any "unreasonable difference" in rates "as between localities or as between classes of service." *Ibid.*

Proposed rate changes must, of course, be filed with the Commission and rates may not be changed except with Commission approval upon thirty days' notice to the Commission and the public. 15 U.S.C. §717c(d). For "good cause shown," the Commission may

> allow changes to take effect without requiring the thirty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

Ibid.

Consistent with these statutory provisions, this Court has developed and applied the "filed rate doctrine" which "prohibits a federally regulated seller of natural gas from charging rates higher than those filed with the Federal Energy Regulatory Commission . . . . " *Arkansas Louisiana Gas Co. v. Hall* (*Arkla*), 453 U.S. 571, 573 (1981). According to the Court, "the right to a reasonable rate is the right to a rate which the Commission files or fixes." *Montana-Dakota Utilities Company v. Northwestern Public Service Company*, 341 U.S. 246, 251-52 (1951). As a result, both the Commission and the courts lack authority to

change rates retroactively. The rule thus "bars 'the Commission's retroactive substitution of an unreasonably high or low rate with a just and reasonable rate.' " *Arkla*, 453 U.S. at 578, *quoting City of Piqua v. FERC*, 610 F.2d 950, 954 (D.C. Cir. 1979). Summarizing the rule, this Court has stated that:

> the Act bars a regulated seller of natural gas from collecting a rate other than the one filed with the Commission and *prevents the Commission itself from imposing a rate increase for gas already sold.*

Arkla, 453 U.S. at 578. (Emphasis added.)

The filed rate doctrine had its origins in this Court's cases interpreting the Interstate Commerce Act, *see, e.g., Lowden v. Simonds-Shield-Lonsdale Grain Co.*, 306 U.S. 516, 520-21 (1939); *Pennsylvania R. Co. v. International Coal Co.*, 230 U.S. 184, 196-97 (1913), "and has been extended across the spectrum of regulated utilities." *Arkla*, 453 U.S. at 577. Its long-standing application by this and other courts has made it an integral part of the NGA.

Just last term this Court revisited and reaffirmed its traditional view of the filed rate doctrine in *Maislin*. In its ruling reversing the Interstate Commerce Commission (ICC), the Court adhered strictly to the principles discussed above. The *Maislin* case dealt with the ICC's application of its Negotiated Rates policy. In its order enunciating that policy, the ICC discussed a growing trend in the motor carrier industry for carriers and shippers to negotiate rates lower than those on file with the ICC. The ICC ruled that the shippers would not be required to pay the tariffed rate concluding that, under such circumstances, "it could be fundamentally unfair not

to consider a shipper's equitable defenses to a claim for undercharges." *NITL – Petition to Institute Rulemaking on Negotiated Motor Common Carrier Rates (Negotiated Rates I)*, 3 I.C.C.2d 99, 103 (1986).

The ICC's ruling was based on its conclusion that the passage of the Motor Carrier Act of 1980, which significantly deregulated the motor carrier industry, justified departure from strict adherence to the filed rate requirement. The ICC ruled that the new competitive atmosphere in the industry was sufficient to deter discrimination. 3 I.C.C.2d at 106. The ICC clarified its new policy in *NITL – Petition to Institute Rulemaking on Negotiated Motor Common Carrier Rates (Negotiated Rates II)*, 5 I.C.C.2d 623 (1989). The Commission explained that its policy did not recognize "equitable defenses" but rather applied the "affirmative statutory requiremen[t] and obligatio[n]" of the Interstate Commerce Act that a carrier's practices be reasonable. 5 I.C.C.2d at 631 n. 18. The Commission stated that it was finding it to be an unreasonable practice for carriers to negotiate rates with customers, not publish the rates and later demand payment at the tariffed rates after service had been rendered. 5 I.C.C.2d at 628 n. 11.

On appeal, the Court followed its traditional view of the filed rate doctrine and ruled that the ICC's abandonment of strict adherence to it was unlawful. The Court relied in part on the "classic statement" of the doctrine as explained in *Louisville & Nashville R. Co. v. Maxwell*, 237 U.S. 94 (1915). As the Court there stated:

> Under the Interstate Commerce Act, the rate of the carrier duly filed is the only lawful charge. Deviation from it is not permitted upon any

> pretext. Shippers and travelers are charged with notice of it, and they as well as the carrier must abide by it, unless it is found by the Commission to be unreasonable.

Ibid. at 97.

The court of appeals properly applied these principles in the case below. SoCal and WNG were on notice of only the rates on file with the Commission when they took service and paid for service under those rates. Under the direct billing mechanism, however, the pipeline obtained authority to impose a retroactive rate alteration upon its customers

> over and above the rates on file at the time of the sale, for the gas they had already purchased. However described, this constitutes a retroactive rate increase . . . prohibited by the NGA.

Columbia Gas Transmission Corp. v. FERC (*Columbia I*), 831 F.2d 1135, 1140 (D.C. Cir. 1987); *see also Arkla*, 453 U.S. at 578 n. 8.[3] Consistent with the rigid application of the filed rate doctrine embraced by the *Maislin* Court, the court of appeals properly ruled that the Commission had no authority to retroactively raise Transwestern's rates to SoCal and WNG. *Transwestern Pipeline Co. v. FERC*, 897 F.2d 570, 577 (D.C. Cir. 1990).

B. The Court of Appeals Properly Employed the Applicable Principles of Statutory Construction.

Transwestern correctly indicates that the standard for review in this case is that established by *Chevron, U.S.A.*,

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[3] See discussion of the direct billing mechanism *supra*, at pages 2-4.

Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837 (1984). However, contrary to Transwestern's assertions, the court of appeals' review of the Commission's actions was consistent with the applicable standards of statutory construction.

1. The Filed Rate Doctrine.

The argument made by Transwestern in this case is remarkably similar to that made by the ICC and rejected by the Court in *Maislin*. In that case, the ICC argued that its decision to abandon the filed rate doctrine was justified by changes in the industry which it regulated and that the ICC was, under the *Chevron* rule, entitled to deference since the Act did not "specifically address the types of practices that are to be considered unreasonable and because its construction is rational and consistent with the statute." *Maislin*, 110 S. Ct. at 2768. The Court rejected this argument. Since Congress had not diverged from the strict interpretation of the filed rate doctrine traditionally followed by the Court, it refused to revisit its prior interpretations of the rule. *Ibid.*[4]

Since the filed rate doctrine under the NGA is rooted in the Interstate Commerce Act, *Arkla*, 453 U.S. at 577, the Court's logic in *Maislin* is equally applicable here. The

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[4] The Court cited its decision in *California v. FERC*, 109 S. Ct. 2024, 2029 (1990), in which it recognized the respect the "Court must accord to long-standing and well-entrenched decisions, especially those interpreting statutes that underlie complex regulatory regimes."

Court's long-standing interpretation of the filed rate doctrine is so deeply ingrained in the NGA that the Commission's contrary interpretation is simply not permissible since it is inconsistent with the regulatory scheme as Congress enacted it and understood it to function.

Transwestern also argues that the court of appeals failed to give proper deference to the Commission's finding that the pipeline's customers had sufficient notice to overcome the requirements of §4(d) of the NGA and the filed rate doctrine. As the court of appeals found with regard to notice, however, the only notice that Transwestern's customers had prior to the Commission's May 11, 1988 order was that they might be liable for recovery of deferred gas costs through the operation of the Account 191 surcharge if they continued to purchase gas from the pipeline. *Transwestern Pipeline Co. v. FERC*, 897 F.2d at 579-81.

Concerning the filed rate doctrine issue, Transwestern echoes the argument made by the ICC in *Maislin*. On that issue, the pipeline argues that the court of appeals departed from acceptable norms of judicial proceedings by failing to accept "FERC's reasonable and equitable solution to the residual cost responsibility issues left in the wake of the 'open-access' transition." Petition for Writ of Certiorari of Transwestern Pipeline Company (Transwestern Pet.), at 22. To the contrary, application of the *Chevron* test in this case leads to the same conclusion as that reached in *Maislin* – that the Commission's interpretation of the act is impermissible since it would result in the very occurrences which the act was meant to avoid: 1) the application of a rate not on file when the sale occurred; and 2) the imposition of a rate increase for gas already sold. *See Arkla*, 453 U.S. at 578.

2. Waiver of the Filed Rate Doctrine.

Transwestern alleges that the court of appeals' decision "effectively reads out of Section 4(d) of the NGA the express authority vested in FERC to waive the notice requirement." Transwestern Pet., at 22. In fact, by holding that the notice requirement may not be waived, the court below acted consistently with long-standing precedents and kept the Commission from reading *into* the statute an exception to the filed rate doctrine wholly inconsistent with the regulatory scheme.

The jurisprudence concerning the commission's power to waive the filed rate doctrine is quite limited. No court has ever found a general power in the Commission to waive the application of the rule. The courts of appeals have dealt with the issue on several occasions. However, the courts have found waivers to be allowed only in cases in which the parties had agreed to the rates to be effective *before* they were filed with the Commission. *See, e.g., City of Piqua, supra* at 954; *City of Girard v. FERC*, 790 F.2d 919, 922-23 (D.C. Cir. 1986) (in which the court rejected a waiver request due to the lack of an agreement); and *Hall v. FERC*, 691 F.2d 1184, 1192 (5th Cir. 1982).[5] In light of

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[5] It is also clear that the statute allows the Commission to shorten the notice of a rate change to less than the statutorily provided 30 days. 15 U.S.C. §717c(d). For example, for good cause shown, the Commission may allow a rate change to be effective on notice as short as one day. However, the Commission's argument that it may retroactively waive such notice would allow its limited power under this section to swallow the filed rate doctrine.

the Commission's duty to protect consumers from exploitation at the hands of the natural gas companies, *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 610 (1941); *Maryland People's Counsel v. FERC*, 761 F.2d 780, 781 (D.C. Cir. 1985), it would be strange indeed if the Commission could waive the rights of the very customers it is obligated to protect to benefit the companies it is empowered to regulate.

These rulings in these cases are, of course, totally consistent with this Court's ruling in *Arkla*. In that case, the Court recognized that the right to a reasonable rate is the right to pay only rates set by the Commission to have prospective effect. *Arkla*, 453 U.S. at 577, 578.[6] Only by requiring rates to be filed with and approved by the Commission before they are assessed can the mandate of *Arkla* and its progeny be fulfilled. As shown by *Maislin*, strict compliance with the filed rate doctrine continues to be required by this Court.[7]

Finally, the decision of the court of appeals is consistent with the statute. NGA §4 includes recitations that rates must be "just and reasonable," 15 U.S.C. §717c(a), filed with the Commission and available for public

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[6] Admittedly, the Court did suggest that the Commission may "permit a waiver." *Arkla*, 453 U.S. at 577. However, that language was clearly dictum and, in any event, there is no discussion in *Arkla* of the circumstances under which a waiver might be appropriate.

[7] In *Maislin*, the Court reiterated the *Maxwell* Court's statement that the filed rate doctrine is "undeniably strict, and it obviously may work hardship in some cases, but it embodies the policy which has been adopted by Congress." 110 S. Ct. at 2766, *quoting Maxwell*, 237 U.S. at 97.

inspection, 15 U.S.C. §717c(c), and non-discriminatory. 15 U.S.C. §717c(b). The Commission is responsible for ensuring that these provisions of the NGA are followed. Clearly, the drafters of the NGA intended, consistent with practice under the Interstate Commerce Act with which they were familiar when the NGA was adopted, that only rates filed with the Commission may be charged by the companies it regulates.[8]

The interpretation of the filed rate doctrine followed by the court of appeals is consistent with the statute and this Court's view of it. As the Court recognized in *Maislin*, while the Commission

> has both the authority and expertise generally to adopt new policies when faced with new developments in the industry, it does not have the power to adopt a policy that directly conflicts with its governing statute. . . . Generalized congressional exhortations to "increase competition" cannot provide the [Commission] authority to alter the well-established statutory filed rate requirements.

110 S. Ct. at 2770. (Citation omitted.)

Moreover, since the Court's interpretation is of long standing, Congress "must be presumed to have been fully

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[8] The Commission contended and Transwestern now argues that the authority under §4(d) of the Act to waive the 30 day notice provision translates into a power to waive the filed rate doctrine altogether. Given the context of the waiver language, the interpretations of the filed rate doctrine by this and other courts over many years, and the explicit requirement throughout the NGA that rates be on file and open to public inspection, this argument is baseless.

cognizant of this interpretation of the statutory scheme, which had been a significant part of our settled law for over a half a century . . . . " *Square D Co. v. Niagara Frontier Traffic Bureau, Inc.*, 476 U.S. 409, 420 (1986). Since the court of appeals has merely followed the traditional view of the filed rate doctrine which this Court recently reaffirmed in *Maislin*, there is no basis for the granting of a writ.

III. THE COURT OF APPEALS' RULING DOES NOT CONFLICT WITH THE NGPA OR PGA REGULATIONS.

As a further ground for obtaining review by this Court, Transwestern asserts that the court of appeals denied the pipeline its

> statutory entitlement to recovery of gas costs – whether as undercollections recorded in Account No. 191 or otherwise – if it demonstrates that such costs are (i) costs paid for the purchases of natural gas and, (ii) do not exceed the NGPA Title I price ceilings and (iii) are not excessive due to fraud, abuse, imprudence or other grounds.

Transwestern Pet., at 26.

Transwestern's argument is based on misconceptions of both the effect of the ruling of the court of appeals and the meaning of Section 601 of the Natural Gas Policy Act of 1978 (NGPA), 15 U.S.C. §3431. First, the decision below did not bar Transwestern from recovering its deferred gas costs but merely rejected the method selected by the pipeline and approved by FERC. It was up to Transwestern and not the court of appeals to design a legal mechanism for recovery of its deferred gas costs. For

instance, Transwestern could have taken the course adopted by Texas Eastern Transmission Corporation when it proposed its GIC. Texas Eastern kept its PGA in operation thereby eliminating the need to find an alternate method for recovery of its deferred gas costs. *Texas Eastern Transmission Corp.*, 44 FERC ¶61,413, at 62,325 (1988).

Second, while NGPA §601 precludes the Commission or a court from disallowing gas costs which meet the conditions listed by Transwestern, it does not *guarantee* that the costs will be *recovered*. Even if the gas prices paid by the pipeline are legal – and included in the pipeline's rates – whether there will be full recovery of those costs has always been directly affected by the marketability of the pipeline's gas. It was Transwestern's decision to abandon PGA pricing for its gas, based at least in part on its determination of the market risk inherent in PGA versus GIC pricing. Transwestern could have retained its PGA and cleared its Account No. 191 balance by absorbing the amount necessary to arrive at a competitive rate. *See Tennessee Pipeline Company*, 33 FERC ¶61,014 (1985); 33 FERC ¶61,061 (1985). Additionally, Transwestern was not required to apply for or accept a GIC certificate.

Transwestern's allegation that it has a guarantee of gas cost recovery is also at odds with both FERC and court precedent. The Commission has consistently taken the view that a pipeline is entitled not to a *guarantee* that it will recover its costs through commodity charges, but merely a reasonable *opportunity* to do so. *See, e.g., Transwestern Pipeline Co.*, 40 FERC ¶61,324, at 61,994 (1987). The Commission's past rulings on this issue are consistent with decisions by this Court. As it has stated:

> It was noted in the *Hope Natural Gas* case that regulation does not assure that the regulated business [will] make a profit. *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1941); *see FPC v. Natural Gas Pipeline Co.*, 315 U.S. 575, 590 (1942). All that was held was that a company could not complain if the return which was allowed made it possible for the company to operate successfully. . . . The due process clause has been applied to prevent governmental destruction of existing economic values. *It has not and cannot be applied to insure values or to restore values that have been lost by the operation of economic forces.*

Market Street Ry. v. Railroad Comm'n, 324 U.S. 548, 566-67 (1945). (Emphasis added.)

Under the NGPA, pipelines remain at risk for the recovery of their gas costs and, if full inclusion of those costs in rates would make their gas unmarketable, they may be precluded from recovery as a result of market forces. Indeed, Transwestern asserted in its petition that one reason for the growth in the pipelines' Account 191 balances was that their customers ceased taking pipeline gas and purchased less expensive gas at the wellhead. Transwestern Pet., at 6-7. However, just as "[t]here is no evidence that Congress [in enacting the NGPA] had any intent to create . . . a producer-assistance program," *FERC v. Martin Exploration Management Company*, 486 U.S. 204, 210 (1988), there is no evidence that it envisioned the NGPA as a "pipeline-assistance program." Thus, the possibility that Transwestern may not recover all of its gas costs as a result of the court of appeals decision does not establish grounds for review by this Court.

IV. THE COURT OF APPEALS' OPINION IS NOT IN CONFLICT WITH RULINGS BY OTHER FEDERAL COURTS OF APPEALS.

Transwestern argues that the decision below is in conflict with rulings of the U.S. Circuit Courts of Appeals for the Fifth Circuit and Tenth Circuit in *Texas Eastern Transmission Corp. v. FERC* (*Texas Eastern*), 769 F.2d 1053 (5th Cir. 1985), and *Phillips Petroleum Co. v. FERC* (*Phillips*), 902 F.2d 795 (10th Cir. 1990), respectively. In fact, there is no conflict between the court's rulings and the cited cases.

Both *Texas Eastern* and *Phillips* dealt with regulations issued by the Commission outlining the circumstances under which first sellers[9] of natural gas can recover certain "production-related" costs under NGPA §110(a)(2), 15 U.S.C. §3320(a)(2).[10] The issues raised by this appeal – the scope and meaning of the filed rate doctrine and the authority of the FERC to waive the application of that rule – were not advanced by the parties in those cases or addressed by either court.

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[9] "First sales" of natural gas under the NGPA include all sales to any interstate pipeline, intrastate pipeline, or natural gas local distribution company. 15 U.S.C. §3301(21)(A). First sales do not include sales by those entities unless the gas was produced by the interstate pipeline, intrastate pipeline, local distribution company, or an affiliate thereof. 15 U.S.C. §3301(21)(B).

[10] NGPA §110(a)(2) provides that a price paid above the applicable maximum lawful price (MLP) will not be considered to exceed the MLP if the price exceeds the MLP to the extent necessary to recover qualified production-related costs. 15 U.S.C. §3320(a)(2).

The court's ruling in *Texas Eastern* was based on the language of the NGPA. The pipeline and distributor parties argued that production-related cost allowances should only have been allowed from the date of the Commission's order in 1983 establishing their levels and not retroactively from the Commission's 1980 order in which it had announced its intention to establish such allowances. 769 F.2d at 1066. This argument was based on the explicit statutory requirement that producers could recover (over and above the applicable MLP) only those production-related costs "allowed" by the Commission. *Ibid.* The pipelines and distributors argued that prior to the 1983 order, which set the level of recovery, there was no Commission authorization for recovery of those costs and therefore recovery of such costs prior to that order was unlawful. *Ibid.* To this the court responded that the Commission's order allowing retroactivity was a "fair balancing of the various problems involved." *Ibid.* It therefore allowed retroactive recovery as of the date of the Commission's 1980 order, which provided notice to parties. The effect of the filed rate doctrine on retroactivity was never raised.

The *Texas Eastern* court did touch tangentially on the notice issue presented here and ruled in a manner totally consistent with the court of appeals in this case. The producers had argued that the Commission should be required to allow recovery of production-related costs retroactive to the enactment of the NGPA even though the Commission had never given notice that it might take such an action. Rejecting this request, the court stated that "rules of this type should be made retrospective, absent adequate notice only in rare cases" and that this

was not a case in which retroactivity without notice was appropriate. *Ibid.*[11]

Phillips did not address these issues either. The sole "retroactivity" issue addressed in that case was whether the Commission failed to follow the mandate of the court of appeals in *Texas Eastern* by requiring explicit contractual authorization for retroactive recovery of interest on production-related costs. *Phillips*, 902 F.2d at 803-05. The court ruled only that the Commission had acted "reasonably and within its discretion in requiring contract authority for the collection of interest on retroactive fuel and power allowances . . . . " *Ibid.* at 804. Again, there was no discussion of the filed rate doctrine or the Commission's authority to waive it.

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[11] The Commission's own rulings prior to Transwestern's December 1, 1987 filing are consistent with the court of appeals' view of the notice requirement. In *Kentucky West Virginia Gas Co.*, 37 FERC ¶61,310 (1986), the Commission rejected a proposal by a pipeline to direct bill deferred gas costs to its customers. The Commission rejected arguments by the pipeline that, by virtue of its PGA, its customers had advance notice that they would be subject to collection of the pipeline's unrecovered purchased gas costs. The Commission stated that the "general notice of a repricing right" did not provide sufficient notice to the pipeline's customers to allow retroactive billing to them of deferred gas costs. 37 FERC at 61,912-13.

CONCLUSION

The petitions for a writ of certiorari should be denied.

Respectfully submitted,

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October 9, 1990

Supreme Court, U.S.
FILED
OCT 9 1990
JOSEPH F. SPANIOL, JR.
CLERK

Nos. 90-344 and 90-367

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

TRANSWESTERN PIPELINE COMPANY,
Petitioner,
v.
KANSAS POWER AND LIGHT COMPANY, *et al.*,
Respondents.

FEDERAL ENERGY REGULATORY COMMISSION,
Petitioner,
v.
PUBLIC UTILITIES COMMISSION OF CALIFORNIA, *et al.*,
Respondents.

On Petitions for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

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BRIEF OF RESPONDENT THE PROCESS GAS CONSUMERS GROUP IN OPPOSITION

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QUESTION PRESENTED

Whether the Federal Energy Regulatory Commission has the power under the Natural Gas Act, 15 U.S.C. §§ 717, *et seq.* (1988), to permit an interstate pipeline to bill its customers retroactively and without advance notice for gas costs from a prior period.

TABLE OF CONTENTS

	Page
STATEMENT OF THE CASE	1
REASONS FOR DENYING THE WRIT	3
I. THIS CASE INVOLVES A MINOR, ISOLATED MATTER OF NO PRACTICAL SIGNIFICANCE	4
II. THE COURT OF APPEALS' FACTUAL DETERMINATION THAT NOTICE WAS INADEQUATE IS CONSISTENT WITH THE CONSUMER PROTECTION OBJECTIVES OF THE NATURAL GAS ACT	5
III. THE COURT OF APPEALS' OPINION IS NOT IN CONFLICT WITH RULINGS BY OTHER FEDERAL COURTS OF APPEALS	9
IV. THIS COURT SHOULD NOT HOLD THIS CASE SUBJECT TO ITS RULINGS IN *AGD* AND *COLUMBIA*	10
CONCLUSION	12

TABLE OF AUTHORITIES

Cases	Page
Arizona Grocery Co. v. Atchison, T. & S.F. Ry., 284 U.S. 370 (1932)	6
Arkansas Louisiana Gas Co. v. Hall, 453 U.S. 571 (1981)	6
Associated Gas Distributors v. FERC, 893 F.2d 349 (D.C. Cir. 1989) *petitions for cert. filed sub nom. Berkshire Gas Co. v. Associated Gas Distributors*, 59 U.S.L.W. 3001 (U.S. June 20, 1990) (Nos. 89-1988, *et al.*)	10
Atlantic Refining Co. v. Public Service Comm'n of New York, 360 U.S. 378 (1959)	7
Chevron U.S.A. v. Natural Resources Defense Council, 467 U.S. 837 (1984)	7
Columbia Gas Transmission Corp. v. FERC, 831 F.2d 1135 (D.C. Cir. 1987), *reh'g denied*, 844 F.2d 879 (1988)	11
Columbia Gas Transmission Corp. v. FERC, 895 F.2d 791 (D.C. Cir. 1990), *petitions for cert. filed sub nom. Panhandle Eastern Pipe Line Co. v. Columbia Gas Transmission Corp.*, 59 U.S.L.W. 3005 (U.S. June 22, 1990) (Nos. 89-2001, *et al.*)	3
FPC v. Hope Natural Gas Co., 320 U.S. 591 (1944)	7
FPC v. Sierra Pacific Power Co., 350 U.S. 348 (1956)	6
FPC v. Tennessee Gas Transmission Co., 371 U.S. 145 (1962)	6
Maislin Industries, U.S. v. Primary Steel, 110 S.Ct. 2759 (1990)	4, 6, 8
Permian Basin Area Rate Cases, 390 U.S. 747 (1968)	8
Phillips Petroleum Co. v. FERC, 902 F.2d 795 (10th Cir. 1990)	9, 10
Texas Eastern Transmission Corp. v. FERC, 769 F.2d 1053 (5th Cir. 1985), *cert. denied*, 476 U.S. 1114 (1986)	9

TABLE OF AUTHORITIES—Continued

Administrative Decisions	Page
Kentucky West Virginia Gas Co., 37 FERC ¶ 61,310 (1986)	5
Locust Ridge Gas Co., 37 FERC ¶ 61,295 (1986)	5
Western Interstate Gas Co., 34 FERC ¶ 61,122, *reh'g denied in part*, 35 FERC ¶ 61,012 (1986)	5
Statutes and Regulations	
Natural Gas Act:	
Section 4(c), 15 U.S.C. § 717c(c) (1988)	6
Section 4(d), 15 U.S.C. § 717c(d) (1988)	6
Natural Gas Policy Act of 1978, Section 110, 15 U.S.C. § 3320 (1988)	9
18 C.F.R. § 154.305 (1990)	2
18 C.F.R. § 154.305(d) (1990)	5

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Respondents.

On Petitions for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

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BRIEF OF RESPONDENT THE PROCESS GAS CONSUMERS GROUP IN OPPOSITION

STATEMENT OF THE CASE

On May 11, 1988, the Federal Energy Regulatory Commission ("FERC") approved Transwestern Pipeline Company's ("Transwestern") application to implement a gas inventory charge ("GIC") which included a proposal to eliminate the pipeline's purchased gas adjustment ("PGA") clause and to direct bill its customers for any

negative balances remaining in its Account 191.[1] Pursuant to that authorization, Transwestern billed certain amounts to Williams Natural Gas Company, an interstate pipeline which was in turn allowed to recover the amounts from Respondent The Kansas Power and Light Company ("KPL")[2] and from Southern California Gas Company, a local distribution company regulated by Respondent Public Utilities Commission of the State of California ("CPUC").[3] These charges are ultimately passed through to retail gas consumers, including members of Respondent The Process Gas Consumers Group.

Under FERC's PGA regulations, interstate pipelines, such as Transwestern, project their future purchased gas costs. The difference between these *projected* costs (which are publicly filed as part of the pipeline's tariff) and the costs actually incurred are booked in the pipeline's Account 191.[4] Ordinarily, Account 191 balances are cleared through credits or surcharges applied to the projected gas costs in succeeding PGA periods. For Transwestern, however, FERC approved a different, non-PGA method of recovery. Because the pipeline had elected to eliminate its PGA (in connection with its voluntary application for a GIC), FERC allowed it to use a direct billing scheme to clear its Account 191 of its unrecovered gas costs. Under this direct billing method, Transwestern assigned cost responsibility to its customers on the basis of their respective sales entitlements.

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[1] *Transwestern Pipeline Co.*, 43 FERC ¶ 61,240, *order on reh'g*, 44 FERC ¶ 61,164 (1988).

[2] KPL is a natural gas local distribution company doing business in the states of Kansas, Missouri, and Oklahoma.

[3] CPUC is a state agency charged with protecting the interests of natural gas consumers throughout California.

[4] A pipeline's effective gas rate at any given time reflects its current estimated cost of gas plus a series of surcharges or credits representing prior period adjustments. *See* 18 C.F.R. § 154.305 (1990).

The court of appeals concluded that the filed rate doctrine bars Transwestern's collection of the unrecovered purchased gas costs in Account 191 which had accrued before May 11, 1988, the date of FERC's order approving the pipeline's direct billing mechanism.[5] Recovery of costs accrued before that date was properly held to be barred because, prior to FERC's order, customers had "no meaningful notice" of the charge. *Transwestern Pipeline Co. v. FERC*, 897 F.2d 570, 581 (D.C. Cir. 1990). The court of appeals rejected FERC's claim of authority to waive the filed rate doctrine, relying in part on the decision by another panel of the D.C. Circuit in *Columbia Gas Transmission Corp. v. FERC* (*"Columbia"*).[6]

REASONS FOR DENYING THE WRIT

There is no basis for Petitioners' attempt to cast FERC's orders below expansively as a key part of the regulatory and market "sea change" in the natural gas industry in recent years. In fact, the challenged ruling of the court below concerns only a minor aspect of one pipeline's election to terminate its PGA. There is neither any reason to believe that the issue, which the pipeline itself could have avoided, is of major practical importance even to the parties, nor any reason to assume that other pipelines have faced or will face similar issues.

The D.C. Circuit's decision rests on a fact-specific determination as to the adequacy of the notice afforded consumers in the unique circumstances of Transwestern's voluntary termination of its PGA. The case involves no new principle of statutory construction nor any other issue of industry-wide significance.

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[5] The court found "no bar" under the filed rate doctrine to the recovery of costs accrued after May 11, 1988. 897 F.2d at 580 n.7.

[6] 895 F.2d 791 (D.C. Cir. 1990), *petitions for cert. filed sub nom. Panhandle Eastern Pipe Line Co. v. Columbia Gas Transmission Corp.*, 59 U.S.L.W. 3005 (U.S. June 22, 1990) (Nos. 89-2001, *et al.*).

The decision of the court of appeals—that FERC may not retroactively impose a different rate from the one on file at the time gas is sold—is wholly consistent with numerous decisions of this Court applying the filed rate doctrine. It properly recognizes that FERC cannot escape its statutory mandate to provide consumers with advance notice of rate changes simply by labelling its actions "policy" initiatives. An agency "does not have the power to adopt a policy that directly conflicts with its governing statute." *Maislin Industries, U.S. v. Primary Steel*, 110 S.Ct. 2759, 2770 (1990) ("*Maislin*").[7]

In sum, the D.C. Circuit's decision does not warrant the exercise of certiorari jurisdiction.

I. THIS CASE INVOLVES A MINOR, ISOLATED MATTER OF NO PRACTICAL SIGNIFICANCE.

As the court of appeals noted, this case was originally selected by the parties to decide a major issue of regulatory policy—the GIC. Importantly, however, "most of the key issues in this case have been rendered moot" and only "peripheral issues survive." 897 F.2d at 573-74.

The "peripheral issue" presented by Petitioners here is whether an as-yet-undetermined amount of Transwestern's deferred gas costs—*i.e.*, those arising before the date (May 11, 1988) that FERC granted Transwestern's request to change the method by which such costs were traditionally recovered—are ineligible for collection under the FERC-approved methodology because of inadequate notice. In fact, the record does not show whether there are any such deferred costs.

Moreover, this case involves unique circumstances that are unlikely to be repeated. Transwestern was not required to terminate its PGA as a condition for institut-

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[7] Although *Maislin* arose under the Interstate Commerce Act, rather than the Natural Gas Act, its holding is equally applicable here. FERC, like the ICC, has no authority "to alter the well-established statutory filed rate requirements." 110 S.Ct. at 2770.

ing a GIC. Thus, despite claims to the contrary by Transwestern (Pet. at 18) and the Acting Solicitor General (Pet. at 9), allowing the decision below to stand will not affect any of the fundamental issues now confronting the natural gas industry. FERC and the pipeline remain free to pursue any lawful means by which the disallowed costs may be recovered in future rates.

II. THE COURT OF APPEALS' FACTUAL DETERMINATION THAT NOTICE WAS INADEQUATE IS CONSISTENT WITH THE CONSUMER PROTECTION OBJECTIVES OF THE NATURAL GAS ACT.

It is significant that Petitioners have not disputed the D.C. Circuit's finding that the rates approved here were, in part, retroactive. Instead, their arguments focus on the court's ruling that customers had not been provided sufficient notice of the rate change to justify an earlier effective date.[8] As these arguments acknowledge, the basis for the decision below was the court's analysis of FERC's position that the statutory notice requirement had been satisfied by the Commission's 1972 general PGA regulations and by two 1986 decisions that did not even involve Transwestern.[9] Thus, notwithstanding Pe-

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[8] As the court of appeals correctly recognized, under FERC's PGA regulations, a pipeline customer normally is not responsible for deferred gas costs once it leaves the pipeline's system; it pays only the filed rates in effect at the time it is being served. 897 F.2d at 580, citing *Kentucky West Virginia Gas Co.*, 37 FERC ¶ 61,310 at 61,912 (1986).

Traditionally, overrecoveries or underrecoveries attributable to gas purchased by *former* customers are treated no differently than other deferred costs. By industry practice and the operation of the PGA regulations, all such deferred costs are included as a surcharge on future rates and recovered through customers' prospective purchases only. *See* 18 C.F.R. § 154.305(d).

[9] Those decisions were *Western Interstate Gas Co.*, 34 FERC ¶ 61,122, *reh'g denied in part*, 35 FERC ¶ 61,012 (1986) and *Locust Ridge Gas Co.*, 37 FERC ¶ 61,295 (1986). The court of appeals did not address arguments, made for the first time in petitions for

titioners' grand characterizations, this case does not pose important legal questions concerning the scope of the filed rate doctrine. Rather, it presents a perfectly ordinary, non-recurring, fact-specific question of whether adequate notice was given as required by the filed rate doctrine and by the explicit provisions of Section 4(d) of the Act. That, we submit, is not a question calling for this Court's attention.

As this Court has long recognized, FERC has no power to change rates retroactively; rather, it is "limited to prescribing the rate 'to be thereafter observed' and thus can effect no change prior to the date of the order." *FPC v. Sierra Pacific Power Co.*, 350 U.S. 348, 353 (1956). "[T]he Act bars a regulated seller of natural gas from collecting a rate other than the one filed with the Commission and prevents the Commission itself from imposing a rate increase for gas already sold." *Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571, 578 (1981) (*"Arkla"*). *See also FPC v. Tennessee Gas Transmission Co.*, 371 U.S. 145, 152-53 (1962). The decision below is consistent with, and mandated by, this Court's decisions interpreting the Act and applying the filed rate doctrine.

The filed rate doctrine is embodied in Sections 4(c) and (d) of the Act. The requirement for advance notice of rate changes is explicit in Section 4(d): "notice shall be given"; there must be "public" posting; the proposed change must be stated "plainly." 15 U.S.C. § 717c(d). These requirements reflect the fundamental purpose of the filed rate doctrine, which is "to render rates definite and certain." *Arizona Grocery Co. v. Atchison, T. & S.F. Ry.*, 284 U.S. 370, 384 (1932), quoted in *Maislin*, 110 S.Ct. at 1766. That purpose is essential to the consumer protection objectives of the Act.

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rehearing, that notice was provided by Transwestern's December 1987 filing proposing the charge. *See* Transwestern App. at 26a.

As this Court has stated, the Act was designed to "protect the consumer interests against exploitation at the hands of private natural gas companies," *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 612 (1944), affording "a complete, permanent and effective bond of protection from excessive rates and charges." *Atlantic Refining Co. v. Public Service Comm'n of New York*, 360 U.S. 378, 388 (1959). Certiorari is not required to confirm the wholly conventional premise underlying the D.C. Circuit's decision here—*i.e.*, that the filed rate doctrine bars FERC from imposing rate changes without proper notice to consumers.

Transwestern (Pet. at 17-22) attempts to frame this case as one in which the agency's interpretation of its governing statute is entitled to special deference under *Chevron U.S.A. v. Natural Resources Defense Council*, 467 U.S. 837 (1984) (*"Chevron"*). Such efforts, though understandable, are misplaced. Not even the Acting Solicitor General has invoked *Chevron* here, because this case involves not statutory interpretation, but rather the correctness *vel non* of FERC's determination that sufficient notice had, in fact, been given.[10] As Transwestern's own extensive argument makes clear, the court of appeals focused precisely on the *adequacy* of notice, based on its examination of the agency record below. The pipeline's ironic complaint that the D.C. Circuit's analysis is "irrelevant and tedious" (Transwestern Pet. at 27) does not change the factual nature of this inquiry. In any event, *Chevron* does not require deference to agency orders that hinge on erroneous factual conclusions or that contravene the purpose and intent of the statute itself.

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[10] Citing *Chevron*, the court of appeals itself acknowledged that, had FERC explicitly approved a rate and stated when that rate would take effect, the court could not have intruded in FERC's province. 897 F.2d at 578. But the court concluded that such deference was *not* warranted where FERC clearly failed to satisfy the Act's notice requirements.

Transwestern's emphasis on the alleged just and reasonable "end result" of FERC's orders (Pet. at 17, citing *Hope*, *supra*) provides no basis for arguing that the court of appeals should not have addressed whether the rates in question complied with the filed rate doctrine.[11] In fact, the D.C. Circuit acted well within its power to determine whether the agency abused its authority, notwithstanding claims that the end result, however achieved, was reasonable. *See Permian Basin Area Rate Cases*, 390 U.S. 747, 791-92 (1968) (the responsibility of the reviewing court is to ensure that the Commission has not "abused or exceeded its authority").

Finally, Transwestern's complaint (Pet. at 26-27) that the D.C. Circuit's decision conflicts with the Natural Gas Policy Act ("NGPA") and FERC's PGA regulations is misplaced. Nothing in the NGPA or the PGA regulations either (1) creates an "entitlement" (Pet. at 26) to the recovery of gas costs in contravention of the Natural Gas Act's notice requirements or (2) protects Transwestern from the consequences of its own decisions. Transwestern *voluntarily* applied for and accepted a GIC certificate, giving its customers the right not to purchase any more gas under the PGA. That customers did what the pipeline invited them to do fails to establish Transwestern's "entitlement" to cost recovery. Moreover, the court of appeals found only that certain costs could not be collected under the mechanism before it; the decision in no way prevents Transwestern from proposing a lawful procedure for recovering any deferred costs it may have incurred before the May 11, 1988 date of FERC's order. And, as previously noted, the record does not show whether there are any such costs.

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[11] In *Maislin*, this Court rejected similar efforts to override the filed rate doctrine. The Court there was unpersuaded by the ICC's labelling the carrier's conduct an "unreasonable practice," since the agency's action was "flatly inconsistent with the statutory scheme as a whole." 110 S.Ct. at 2768.

III. THE COURT OF APPEALS' OPINION IS NOT IN CONFLICT WITH RULINGS BY OTHER FEDERAL COURTS OF APPEALS.

Transwestern argues that the decision below is in conflict with rulings of the U.S. Courts of Appeals for the Fifth and Tenth Circuits in *Texas Eastern Transmision Corp. v. FERC*, 769 F.2d 1053 (5th Cir. 1985), *cert. denied*, 476 U.S. 1114 (1986) and *Phillips Petroleum Co. v. FERC*, 902 F.2d 795 (10th Cir. 1990), respectively. Those decisions uphold FERC orders authorizing the collection of certain production-related costs under NGPA Section 110. 15 U.S.C. § 3320 (1988). In fact, however, there is no conflict among the circuits on the issue at bar.

In *Texas Eastern*, the court found that "purchasers *were on notice* as of 1980" (through FERC's Order 94 rulemaking) of the date when production-related costs would be assessed, even though they were not on notice as to the precise amount of the charge. 769 F.2d at 1066, 1060 n.8 (emphasis added). Here, by contrast, the court of appeals—considering an entirely different series of FERC orders and regulations—found "no meaningful notice in any Commission act before May 11, 1988." 897 F.2d at 581. Even more importantly, in *Texas Eastern*, the Fifth Circuit specifically rejected arguments that rate increases should be allowed as of an earlier date, citing "the purchasers' need for notice." 769 F.2d at 1066. Instead of creating a conflict with the D.C. Circuit, the Fifth Circuit's ruling in *Texas Eastern* lends additional support to the decision challenged here.

Since the Tenth Circuit in *Phillips* never discussed the filed rate doctrine, it is difficult to ascertain any pertinent conflict with the D.C. Circuit's decision. That case was limited to the issue of "whether the Commission followed the *Texas Eastern* mandate." 902 F.2d at 799. The Tenth Circuit's decision had nothing to do with the PGA regulations or agency orders construed here. The

only instance in which the court of appeals there addressed the matter of notice involved FERC's 1987 decision to require producers to have had contractual authority in 1983 to be eligible to collect interest for certain fuel and power allowances. Again, unlike the situation here, the court there found that producers had indeed been "on notice" in 1983 that interest on production-related costs would be allowed only if contractually authorized. 902 F.2d at 804.

The lack of any conflict among the circuits is further shown by the fact that the Acting Solicitor General does not support Transwestern's claim of such conflict.

IV. THIS COURT SHOULD NOT HOLD THIS CASE SUBJECT TO ITS RULING IN *AGD* AND *COLUMBIA*.

The Acting Solicitor General has requested that this case be held for disposition in light of the petitions for certiorari filed in *Associated Gas Distributors v. FERC* (*"AGD"*)[12] and *Columbia*. This request should be denied because the issues in those cases are entirely different.

Unlike this case, which hinges on a straightforward factual determination of whether or not consumers were given adequate notice of a rate increase, *AGD* addresses the issue of whether the rate methodology approved by FERC constituted a retroactive rate increase. Here the petitions argue that customers had notice that they were responsible for paying the costs at issue; in contrast, no petitioner in *AGD* claims that customers knew they would be assessed additional charges for gas which they had purchased years earlier. Thus, there is nothing in the grounds asserted for review of *AGD* to suggest that any foreseeable disposition of that case would affect the holding of the court of appeals in this case.

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[12] 893 F.2d 349 (D.C. Cir. 1989) *petitions for cert. filed sub nom. Berkshire Gas Co. v. Associated Gas Distributors*, 59 U.S.L.W. 3001 (U.S. June 20, 1990) (Nos. 89-1988, *et al.*).

There is even less reason for holding this case pending disposition of *Columbia*. The Acting Solicitor General did not seek plenary review of *Columbia*, requesting instead that it be held for disposition in light of *AGD* (Pet. in No. 90-131 at 18). The Brief for Certain Respondents in Opposition (at pp. 22-23) pointed out the lack of merit in that request for a hold.

There is even less basis for a hold in this case. *Columbia* involves FERC's claim that its statutory authority to waive the Act's 30-day prior notice requirement allows it to impose higher rates for gas purchased by customers many years earlier. Importantly, certiorari was *not* sought with respect to the D.C. Circuit's earlier decision rejecting FERC's claim that adequate notice of this rate increase had been provided through the Order 94 rulemaking process.[13] Thus, the adequacy-of-notice issues which are at the heart of the instant case are not present in *Columbia*. Finally, although FERC did claim in both cases that it could waive the 30-day prior notice provision in the Act, the circumstances assertedly justifying waiver in the two cases are entirely different. As the court of appeals noted, FERC's waiver claim here was "a last stand," and it was questionable whether that claim had any "remaining life" since it applied only to the costs, if any, incurred before the May 11, 1988 date of FERC's order. 897 F.2d at 580 n.7.

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[13] *Columbia Gas Transmission Corp. v. FERC*, 831 F.2d 1135 (D.C. Cir. 1987), *reh'g denied*, 844 F.2d 879 (1988).

CONCLUSION

For the reasons stated, the petitions for Writ of Certiorari should be denied.

Respectfully submitted,

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October 9, 1990

Supreme Court, U.S.
FILED
OCT 19 1990
JOSEPH F. SPANIOL, JR.
CLERK

Nos. 90-344 and 90-367

IN THE
Supreme Court of the United States
OCTOBER TERM, 1990

TRANSWESTERN PIPELINE COMPANY,
Petitioner,
v.
KANSAS POWER AND LIGHT COMPANY, *et al.*,
Respondents.

FEDERAL ENERGY REGULATORY COMMISSION,
Petitioner,
v.
PUBLIC UTILITIES COMMISSION OF CALIFORNIA, *et al.*,
Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

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REPLY BRIEF OF TRANSWESTERN PIPELINE COMPANY

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RULE 29.1 STATEMENT

The listing of Petitioner Transwestern Pipeline Company's parent company and its subsidiaries was provided on pages iii-ix of the petition for a writ of certiorari in No. 90-344. The following companies should be added to the list of subsidiaries of Enron Corp.:

Enron Gas Liquids Holding B.V. (The Netherlands)

Enron Gas Liquids B.V. (The Netherlands)
Loga Chemicals B.V. (The Netherlands)

Enron Argentina, S.A. (Argentina)
Enron Milford, Inc. (Delaware)
Enron Power Operations Limited (England)
Enron Power Construction Limited (England)
Teeside Power Limited (United Kingdom)
Enron Storage Company (Delaware)
Enron Gas Processing (U.K.) Limited (United Kingdom)

The following entities should be added to the list of joint ventures of Enron Corp.:

Bannon International Limited (Liberia)

Owned by Enron Gas Liquids, Inc.—50%
Subsidiaries:

Mundogas Shipping Ltd. (Liberia)

Mundogas America Limited (Liberia)
Mundogas Europe Limited (Liberia)
Mundogas Orinoco Limited (Liberia)
Mundogas Pacific Limited (Liberia)
Mundogas Transportation Limited (England)

Enron Arbross Ship Management Co. Ltd. (Hong Kong)

Owned by Enron Gas Liquids, Inc.—50%

Halton International Limited (Liberia)

Owned by Enron Gas Liquids, Inc.—50%
Subsidiaries:

Mundogas (Storage) Inc. (Liberia)
Mundogas (UK) Ltd. (England)
Mundogas Limited (Liberia)
Mundogas Services Limited (Liberia)
Mundogas Trading Limited (Liberia)

Tarumi Enterprises Ltd. (Liberia)

Owned by Enron Gas Liquids, Inc.—50%
Subsidiaries:

Veldmoor International Limited (Liberia)
Weddell Corporation (Liberia)

TABLE OF CONTENTS

	Page
INTRODUCTION	1
SUMMARY OF ARGUMENT	1
ARGUMENT	2
A. The Lower Court Erred In Substituting Its Statutory Interpretation For That Of The FERC	2
B. FERC Does Possess The Statutory Authority To Waive The "Filed Rate" Doctrine	5
C. The *Maislin* Decision Did Not Eliminate FERC's Statutory Waiver Authority Under The NGA	6
D. The Lower Court's Decision Conflicts With The Requirements Of The NGPA	6
E. The Lower Court's Decision Conflicts With Decisions Of Other Circuits	8
F. The Court's Decision In *AGD II* Is Not Dispositive Here	9
CONCLUSION	10

TABLE OF AUTHORITIES

Cases Page

Arkansas Louisiana Gas Co. v. Hall, 453 U.S. 571 (1981) 5

Associated Gas Distributors v. FERC, 893 F.2d 349 (D.C. Cir. 1989), *reh'g denied*, 898 F.2d 809 (D.C. Cir.), *cert. denied*, 59 U.S.L.W. 3277 (U.S. Oct. 9, 1990) (No. 89-2016) 9-10

Associated Gas Distributors v. FERC, 810 F.2d 226 (D.C. Cir. 1987) 7

Chevron U.S.A. Inc. v. NRDC, Inc., 467 U.S. 837 (1984) ..... *passim*

City of Piqua v. FERC, 610 F.2d 950 (D.C. Cir. 1979) 5, 9

Hall v. FERC, 691 F.2d 1184 (5th Cir. 1982), *cert. denied*, 464 U.S. 822 (1983) 9

Maislin Industries, U.S., Inc. v. Primary Steel, Inc., 110 S. Ct. 2759 (1990) 2, 6

Permian Basin Area Rate Cases, 390 U.S. 747 (1968) 7

Phillips Petroleum Co. v. FERC, 902 F.2d 795 (10th Cir. 1990) 8

Public Service Co. of New Hampshire v. FERC, 600 F.2d 944 (D.C. Cir.), *cert. denied*, 444 U.S. 990 (1979) 4, 8

Texas Eastern Transmission Corp. v. FERC, 769 F.2d 1053 (5th Cir. 1985), *cert. denied sub nom. Associated Gas Distributors v. FERC*, 476 U.S. 1114 (1986) 8

Towns of Concord and Wellesley v. FERC, 844 F.2d 891 (1st Cir. 1988) 9

Transwestern Pipeline Co. v. FERC, 897 F.2d 570 (D.C. Cir. 1990) 9, 10

Statutes

Natural Gas Act, 15 U.S.C. §§ 717, *et seq.*
15 U.S.C. § 717c ..... *passim*

Natural Gas Policy Act, 15 U.S.C. §§ 3301, *et seq.*
15 U.S.C. § 3431 ..... *passim*

TABLE OF AUTHORITIES—Continued

Administrative Decisions Page

Transwestern Pipeline Co.

43 F.E.R.C. ¶ 61,240 (1988) 4
44 F.E.R.C. ¶ 61,164 (1988) 4, 6
49 F.E.R.C. ¶ 61,436 (1989) 6
50 F.E.R.C. ¶ 61,427 (1990) 6

REPLY BRIEF OF TRANSWESTERN PIPELINE COMPANY

INTRODUCTION

Transwestern Pipeline Company ("Transwestern") hereby replies to the briefs in opposition filed by the Process Gas Consumers Group ("PGC") and the Kansas Power and Light Company ("KP&L") jointly with the Public Utilities Commission of the State of California ("CPUC") on October 9, 1990.

SUMMARY OF ARGUMENT

Respondents' briefs in opposition confirm that the questions presented by the petitions for a writ of certiorari are worthy of review. Respondents fail to reconcile the standards of *Chevron U.S.A. Inc. v. NRDC, Inc.*, 467 U.S. 837 (1984) (*"Chevron"*) with the lower court's substitution of its own narrow and inflexible "notice" interpretation for the Federal Energy Regulatory Commission's ("FERC") interpretation of what constitutes acceptable "notice" under Section 4(d) of the Natural Gas Act ("NGA"), 15 U.S.C. § 717c(d), and with the limits placed by the lower court on the scope of FERC's waiver authority under the same statutory provision. Transwestern submits that *Chevron* requires deference to FERC's attempt to interpret the statute it has been empowered to administer by Congress. The lower court's decision does not grant such deference to FERC.

Respondents have likewise failed to reconcile the conflict inherent between the lower court's decision and the Congressional mandate reflected in Title VI of the Natural Gas Policy Act ("NGPA"), 15 U.S.C. §§ 3431, *et seq.*, regarding a pipeline's right, under certain circumstances, to recovery of gas costs. Given their resulting inability to defend this conflict as lawfully permissible, respondents assert that Transwestern is seeking a recovery right beyond the express terms of the NGPA. Such is not the case. All Transwestern seeks is the right expressly pro-

vided by the NGPA and NGA—the right to seek recovery from its sales customers of purchased gas costs.

Respondents suggest that the Court's recent decision in *Maislin Industries, U.S., Inc. v. Primary Steel, Inc.*, 110 S. Ct. 2759 (1990), ("*Maislin*") supports the lower court's decision. As this Court is well aware, however, *Maislin* did not involve either review of a lower court decision which imposed a notice date different from that imposed by the agency, or review of an agency interpretation of the scope of its waiver authority.

Finally, PGC urges that this Court deny the petitions because "this case involves a minor, isolated matter of no practical significance." PGC Brief at 4. As indicated in the "Motion for Leave to File Brief Amicus Curiae and Brief Amicus Curiae on Behalf of the Interstate Natural Gas Association of America in Support of Petitioners", filed October 9, 1990, nothing could be further from the truth. For five years now FERC has grappled with the consequences of its efforts to increase competition within the natural gas industry. FERC's orders reviewed below are an outgrowth of the major policy initiatives FERC enunciated in its Order Nos. 436, 451 and 500, and represent FERC's initial efforts under its Order No. 500 gas inventory charge policies to provide "open-access" transportation without a build-up of future take-or-pay. Such issues are not trivial—either in the magnitude of dollars at stake for the natural gas industry or in the direction the industry will take in responding to the combination of future market and regulatory forces.

ARGUMENT

A. The Lower Court Erred In Substituting Its Statutory Interpretation For That Of The FERC

The court below disallowed Transwestern's collection of purchased gas costs based upon the court's interpretation of the "filed rate" doctrine. According to the lower court, the "notice" afforded to Transwestern's customers through FERC regulations and Transwestern's tariff

(and found by FERC to satisfy the NGA Section 4(d) requirement for purposes of assessing cost responsibility for deferred gas costs) was inadequate under the "filed rate" doctrine. The rejection of FERC's notice findings, in favor of the court's own determination of what constituted adequate NGA Section 4(d) notice, was endorsed by both briefs in opposition as consistent with the principles of *Chevron*.

Arguments concerning this asserted notice defect and, ergo, the alleged failure of FERC to properly interpret the "filed rate" doctrine, quickly unravel when considered in the context of the regulatory and statutory system in place for recovery of purchased gas costs and the teachings of *Chevron*. As to the regulatory scheme, Transwestern's tariff—like that of most other interstate pipelines—permitted refunds to (or collection from) jurisdictional sales customers of past period overrecovered (or underrecovered) purchased gas costs by way of incremental credits (or surcharges) on projected jurisdictional sales. This crediting/surcharge mechanism (which is an integral component of the purchased gas adjustment ("PGA") clause implemented in 1972) was designed to keep both a pipeline and its sales customers whole with respect to the gas cost component of a pipeline's rates, and was necessary because of the errors inherent in the method by which this cost component is derived—*i.e.* based upon estimates of the levels and costs of expected purchases and estimates of projected sales.

Moreover, the method by which Transwestern is to recover the purchased gas costs in question arose (and was approved) not as a result of an NGA Section 4 tariff filing, but rather in the context of (1) the termination of Transwestern's jurisdictional sales services on behalf of its two principal customers, (2) the concomitant initiation of firm transportation-only services for one of those customers,[1] and (3) the termination of Transwestern's

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[1] The other sales customer elected to leave Transwestern's system entirely.

PGA tariff clause. *See Transwestern Pipeline Co.*, 43 F.E.R.C. ¶ 61,240, *reh'g granted in part and clarified*, 44 F.E.R.C. ¶ 61,164 (1988), App. 55a-127a. Accordingly, in the orders reviewed by the lower court, FERC quite correctly found that its PGA regulations in this regard, and Transwestern's tariff provisions implemented pursuant to these regulations, provided adequate notice to Transwestern's two principal sales customers that they would remain responsible for all purchased gas costs previously incurred by Transwestern and which remained unrecovered upon termination of the underlying sales services and the PGA clause itself. 44 F.E.R.C. at 61,537, App. 113a.

The arguments of PGC and KP&L/CPUC notwithstanding, the adequacy of notice analysis does indeed invoke the *Chevron* standards for review of agency action. Whether framed in terms of adequacy, timing, or otherwise, the findings of FERC rested upon its interpretation of the statutory NGA Section 4 "notice" requirement, and its construction of this statutory requirement, as it established the right of a regulated entity to charge rates and to recover costs associated with the complete termination of jurisdictional sales services.[2] That the lower court substituted its judgement of what constitutes adequate statutory notice is without question.[3] Nevertheless, in the absence of a specific finding that FERC's interpretation

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[2] Respondents KP&L and CPUC mistakenly assert that "[w]ithout direct billing, [Transwestern] would have sought to recover these costs prospectively as part of its sales commodity rate to its customers." KP&L/CPUC Brief at 2 (emphasis omitted). This assertion defies logic since the underlying sales services terminated—which is why FERC authorized direct billing in the first instance.

[3] Equally without question is the inconsistency between the lower court's findings on adequacy of notice to Transwestern's customers and its prior findings in *Public Service Co. of New Hampshire v. FERC*, 600 F.2d 944 (D.C. Cir.), *cert. denied*, 444 U.S. 990 (1979), that the collection of fuel costs "left over" in the wake of transition from one cost recovery formula to another does not violate the "filed rate" doctrine.

of the notice requirement did violence to the statutory scheme, a finding which Transwestern submits is lacking in the lower court's decision, "the principle of deference to administrative interpretations '[must be] followed by this Court whenever decision as to the meaning or reach of a statute [requires] reconciling conflicting policies . . . .'" *Chevron*, 467 U.S. at 844 (citations omitted). Such deference was not accorded FERC by the lower court in the decision below.

B. FERC Does Possess The Statutory Authority To Waive The "Filed Rate" Doctrine

The *Chevron* deference standards also apply to FERC's construction of its waiver authority and, specifically, its authority to waive, *in toto*, the notice requirement "for good cause shown." Again, respondents ignore the unambiguous words of the NGA and baldly assert that FERC's waiver authority—and the breadth of the "good cause" exception—applies only to notice to FERC, *i.e.*, the ministerial filing requirement itself. *See e.g.* KP&L/CPUC Brief at 13-16. As such, respondents assert that, although a rate change in advance of notice to (by the act of filing with) FERC may be permissible, "notice" to the customers is mandatory and non-waivable.[4] Yet, the statute is clear on its face—what is waivable for "good cause" is the "thirty days' notice to the Commission *and to the public*." 15 U.S.C. § 717c(d) (Emphasis added). And, while good cause for waiver of the *FERC* notice/filing requirement has been found where there has been agreement between the contracting parties, *see City of Piqua v. FERC*, 610 F.2d 950 (D.C. Cir. 1979), nothing in the statute or case law supports the anomalous proposition that, *ipso facto*, there can

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[4] Respondents allege that the decision below comports with the Court's holding in *Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571 (1981). *See* PGC Brief at 6 and KP&L/CPUC Brief, *passim*. In fact, however, on the very waiver argument presented here, the Court left open the issue of whether the "good cause" exception could permit retroactive collection of an unfiled rate. 453 U.S. at 578, n.8.

never be waiver of the notice-to-the-customer requirement, for good cause shown.

C. The *Maislin* Decision Did Not Eliminate FERC's Statutory Waiver Authority Under The NGA

Maislin does not, as respondents suggest, eliminate FERC's statutory waiver authority under NGA Section 4(d). *See* KP&L/CPUC Brief at 13-16. In fact, the Court explicitly declined to "express [any] view today on the validity of [the Interstate Commerce Commission's interpretation of its waiver authority under the Interstate Commerce Act]." *Maislin*, 110 S. Ct. at 2770 n. 14. Rather, *Maislin* merely provides that rates privately negotiated between parties cannot be implemented unless filed with the ICC. In contrast, in the agency orders under review below, FERC permitted Transwestern—as a condition to other NGA authorizations—to make subsequent NGA Section 4 filings to recover (or refund, as appropriate) any amounts remaining in Account No. 191 upon the termination of the underlying sales services.[5] And, in this context, FERC concluded that ample notice of deferred purchased gas cost responsibility was provided through the PGA regulations as well as the surcharge recovery provisions of Transwestern's tariff, and that good cause existed for a waiver of the notice requirements to the extent such waiver was necessary. *See Transwestern*, 44 F.E.R.C. at 61,537, App. 113a. Accordingly, *Maislin* provides no support for respondents' assertions regarding "filed rate" impediments to the direct bill procedure.

D. The Lower Court's Decision Conflicts With The Requirements Of The NGPA

Respondents concede the applicability of the NGPA but attempt to refute—by overstating—Transwestern's argument concerning the "guaranteed passthrough" pro-

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[5] These filings were, of course, noticed and subsequently accepted, subject to refund, in accordance with the requirements of Section 4 of the NGA. *See Transwestern Pipeline Co.*, 49 F.E.R.C. ¶ 61,436 (1989) and 50 F.E.R.C. ¶ 61,427 (1990).

visions of Title VI of the NGPA (specifically Section 601, 15 U.S.C. § 3431).[6] *See e.g.* KP&L/CPUC Brief at 16-18. By expounding on the proposition that gas cost recovery is not subject to absolute, unqualified guarantees—which no one disagrees with—respondents have resorted to classic "straw-man" tactics which, stated politely, miss the mark.

Transwestern has never claimed an unfettered, non-reviewable right to recovery of gas costs. Indeed, FERC's orders under review below only permitted Transwestern to make subsequent NGA Section 4 filings to collect these gas costs. The filings themselves were accepted by FERC, but suspended, to provide parties the right to challenge cost recovery under the applicable standards of the NGA and NGPA—a point respondents ignore.

What respondents also refuse to acknowledge is that the lower court's "filed rate" findings may result in denying Transwestern the right to recover certain gas costs. Under the court's rationale, nothing Transwestern can do today can cure the alleged "notice" deficiency. Thus, the lower court's decision contravenes both the constitutional and NGA/NGPA protections designed to ensure that regulated gas companies are provided a meaningful opportunity to be recompensed in the provision of reliable and continuing services. *See, e.g., Permian Basin Area Rate Cases*, 390 U.S. 747, 791-93 (1968); *see also Associated Gas Distributors v. FERC*, 810 F.2d 226, 233 (D.C. Cir. 1987).

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[6] NGPA Section 601 provides in pertinent part, that

> the Commission may not deny any interstate pipeline recovery of any amount paid with respect to any purchase of natural gas if, under subsection (b) of this section, such amount is deemed to be just and reasonable for purposes of sections 4 and 5 of such Act, except to the extent the Commission determines that the amount paid was excessive due to fraud, abuse, or similar grounds.

15 U.S.C. § 3431(c)(2).

E. The Lower Court's Decision Conflicts With Decisions Of Other Circuits

The inflexible and unnecessarily circumspect "filed rate"/notice analysis applied by the lower court cannot be squared with decisions from other circuits which have considered and rejected similar "filed rate" doctrine attacks on FERC orders. *See Texas Eastern Transmission Corp. v. FERC*, 769 F.2d 1053 (5th Cir. 1985), *cert. denied sub nom. Associated Gas Distributors v. FERC*, 476 U.S. 1114 (1986) and *Phillips Petroleum Co. v. FERC*, 902 F.2d 795 (10th Cir. 1990).[7]

An even more overt conflict exists with respect to the breadth of the Commission's waiver authority under Section 4(d) of the NGA. In this regard, the lower court did not follow its own precedent—and precedents from other circuits—to the extent that its narrow waiver analysis refused to recognize the agreement between Transwestern and its customers, as memorialized in Transwestern's service agreements with its customers (which incorporated all provisions of Transwestern's FERC-approved tariff), permitting recovery of all purchased gas costs (including recovery of unrecovered gas costs through the surcharge provisions). Transwestern's former sales customers agreed to the provisions of Transwestern's PGA mechanism. As such, the PGA clause represents nothing more or less than an agreement which, subject only to the NGPA Title VI requirements, commits Transwestern's customers to reimburse the pipeline for gas costs prudently incurred on their behalf.[8]

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[7] In this regard, the lower court's "filed rate" doctrine analysis conflicts with precedent from the D.C. Circuit. *See Public Service Co. of New Hampshire v. FERC*, 600 F.2d 944 (D.C. Cir.), *cert. denied*, 444 U.S. 990 (1979).

[8] Indeed, the lower court implicitly referenced this agreement, and the obligations imposed thereunder, when it rejected the downstream purchasers' broad attack on the direct bill mechanism (and, specifically, the prospect of Southern California Gas Company being assessed either the whole, or only a part of the Account No. 191 balance) by stating:

The lower court's failure, to permit waiver (to the extent required) of the "filed rate" doctrine based upon prior agreement of the parties stands in conflict with case law from the D.C. Circuit and from decisions of the Fifth and First Circuits, as well. *See City of Piqua v. FERC*, 610 F.2d 950 (D.C. Cir. 1979); *see also Hall v. FERC*, 691 F.2d 1184 (5th Cir. 1982), *cert. denied*, 464 U.S. 822 (1983); *Towns of Concord and Wellesley v. FERC*, 844 F.2d 891, 896-97 (1st Cir. 1988).

F. The Court's Decision In *AGD II* Is Not Dispositive Here

Both briefs in opposition agree that "material differences" between the instant facts and the facts raised by FERC in its certiorari petition, filed June 21, 1990, in *FERC v. Associated Gas Distributors*, Case No. 89-2016 seeking review of the D.C. Circuit's decision in *Associated Gas Distributors v. FERC*, 893 F.2d 349 (D.C. Cir. 1989), *cert. denied*, 59 U.S.L.W. 3277 (U.S. Oct. 9, 1990) (No. 89-2016) ("*AGD II*"), require that Transwestern's certiorari petition be considered on its own merits and independently from the decision in *AGD II*.[9]

The instant case stands in stark contrast to the facts and issues presented in *AGD II* in at least two critical respects. First, there exists no genuine element of retroactivity in the billing procedure under review here. That is, the "past purchase deficiency" methodology—*i.e.* the centerpiece of the *AGD II* appeals—was not at issue in

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> [i]n any event, the first of the options (SoCal bearing the whole charge if it continued to take sales service) was no more than what would have happened under the existing PGA regulations, before the new Transwestern filing, under the same circumstances.

Transwestern Pipeline Co. v. FERC, 897 F.2d 570, 579 (D.C. Cir. 1990), App. 18a.

[9] As stated by PGC, "there is nothing in the grounds asserted for review of [*AGD II*] to suggest that any foreseeable disposition of that case would affect the holding of the court of appeals in this case." PGC Brief at 10.

this case.[10] Second, the costs at issue in the two proceedings are wholly dissimilar. Unlike *AGD II*, the instant appeal deals strictly with Transwestern's right to collect gas costs which, as the lower court acknowledged, would have otherwise been recoverable but for the termination of Transwestern's jurisdictional sales services and related PGA tariff provisions, and the implementation, in lieu thereof, of the direct bill procedure for the recovery of all remaining purchased gas costs. *See Transwestern*, 897 F.2d at 579, App. 18a.

CONCLUSION

For the foregoing reasons and those stated in the petition for a writ of certiorari, the Court should grant the petition for certiorari in No. 90-344.

Respectfully submitted,

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[10] Indeed, nowhere in the opinion below did the court find that the direct bill mechanism (which allocated costs on the basis of contract demand levels) violated the retroactive ratemaking prohibition. And, although the "filed rate" and "retroactive ratemaking" concepts do involve similar considerations—and very often overlap—there are distinctions, apparently recognized by the court below and more directly acknowledged in Judge Williams' concurring opinion denying rehearing and rehearing *en banc* in *Associated Gas Distributors v. FERC*, 898 F.2d 809, 810 (D.C. Cir. 1990). Indeed, while the true-up mechanism inherent in PGA surcharges may operate to effect a collection of past costs, so long as the right to recover such costs (*i.e.* surcharges) is on file with FERC, then no unlawful collection can be found.

No. 90-344 and No. 90-367

MOTION FILED
OCT 9 1990

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

TRANSWESTERN PIPELINE COMPANY,
Petitioner,
v.
KANSAS POWER AND LIGHT COMPANY, *et al.*,
Respondents.

FEDERAL ENERGY REGULATORY COMMISSION,
Petitioner,
v.
PUBLIC UTILITIES COMMISSION OF CALIFORNIA
and KANSAS POWER & LIGHT COMPANY,
Respondents.

On Petitions for Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

MOTION FOR LEAVE TO FILE BRIEF AMICUS CURIAE AND BRIEF AMICUS CURIAE ON BEHALF OF THE INTERSTATE NATURAL GAS ASSOCIATION OF AMERICA IN SUPPORT OF PETITIONERS

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

No. 90-344

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v.

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PUBLIC UTILITIES COMMISSION OF CALIFORNIA and KANSAS POWER & LIGHT COMPANY,
Respondents.

On Petitions for Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

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MOTION FOR LEAVE TO FILE BRIEF AMICUS CURIAE

The Interstate Natural Gas Association of America ("INGAA") respectfully moves pursuant to Rule 37.2 for leave to file the attached brief *amicus curiae* in this case. Petitioners have consented to INGAA's filing of this brief. The consent of respondent, Kansas Power and Light Company, was requested but refused.

STATEMENT OF INTEREST

INGAA is a non-profit national trade association representing virtually all of the major interstate natural gas

transmission companies operating in the United States. The companies account for over 90 percent of all natural gas transported and sold for resale in interstate commerce. INGAA's members also include major Canadian interprovincial pipelines subject to regulation by the National Energy Board of Canada. INGAA's U.S. members are regulated by the Federal Energy Regulatory Commission ("Commission") under the Natural Gas Act ("NGA"), 15 U.S.C. §§ 717 *et seq.* (1988), and, to a lesser extent, under the Natural Gas Policy Act of 1978 ("NGPA"), 15 U.S.C. §§ 3301 *et seq.* (1988).

REASONS FOR GRANTING THE MOTION

This case involves orders of the Commission which permitted a natural gas pipeline to direct bill its customers for the balance remaining in a purchased gas cost account (Account No. 191) when the pipeline terminated the account upon implementation of a gas inventory charge pursuant to the Commission's Order No. 500. 52 Fed. Reg. 30,334, III FERC Stats. & Regs. ¶ 30,761 (1987). The United States Court of Appeals for the District of Columbia Circuit held that notwithstanding the Commission's finding of "good cause" for waiving the notice requirement in Section 4(d) of the NGA, the direct billing by the pipeline of such costs constituted retroactive ratemaking in violation of the filed rate doctrine. *Transwestern Pipeline Co.* v. *FERC*, 897 F.2d 570 (D.C. Cir. 1990).

The issue in this case is therefore similar to the issues presented in *FERC* v. *Associated Gas Distributors, petition for cert. pending*, No. 89-2016 (filed June 21, 1990), in which the Commission has sought review of another D.C. Circuit opinion which held that a Commission order authorizing a pipeline's recovery of take-or-pay costs using the purchase deficiency methodology prescribed in Order No. 500 violated the filed rate doctrine. *Associated Gas Distributors* v. *FERC*, 893 F.2d 349 (D.C. Cir. 1989) ("*AGD II*"). INGAA has filed a motion for leave to file

amicus curiae in support of the Commission's petition for writ of certiorari in that case. Additionally, the issues in this case are similar to those raised by the Commission and certain pipelines in their respective petitions for certiorari in *FERC* v. *Columbia Gas Transmission Corporation, petition for cert. pending*, No. 90-131 (filed July 18, 1990) and *Panhandle Eastern Pipe Line Company* v. *Columbia Gas Transmission Corporation, petition for cert. pending*, No. 89-2001 (filed June 22, 1990). Those petitions seek review of a decision of the D.C. Circuit which held that notwithstanding the Commission's finding that "good cause" existed to waive the notice requirement of NGA Section 4(d), the direct billing by pipelines for certain production costs that the Commission had previously required the pipelines to pay producers for past sales of gas constituted a violation of the filed rate doctrine. *Columbia Gas Transmission Corp.* v. *FERC*, 895 F.2d 791 (D.C. Cir. 1990) (*"Columbia II"*). INGAA has also filed a motion for leave to file *amicus curiae* in support of the petitions for writ of certiorari in that case.

The court of appeals in the case herein, as in *AGD II* and *Columbia II*, has unjustifiably extended the filed rate doctrine and failed to accord proper deference to the ratemaking authority vested in the Commission by Section 4 of the NGA. The result of the court of appeals' actions is to prohibit the collection of prudently incurred purchased gas costs, the recovery of which is guaranteed under Title VI of the NGPA. Moreover, the decision below has the practical effect of thwarting efforts of the entire natural gas pipeline industry to make a full transition to competitive markets and thus to put the economic vestiges of past regulatory schemes behind them. The gas inventory charge mechanism adopted by the Commission's Order No. 500 is an integral part of the Commission's policy for addressing future take-or-pay responsibility in the new competitive environment. The Commission's determination that pipelines may direct bill the balance of gas costs in their Account No. 191 upon implementation of a gas in-

ventory charge is a vital step in the industry's transition process. While the magnitude of such costs varies by pipeline, the costs at issue herein are substantial—as much as several hundred million dollars for a single pipeline.

INGAA, as representative of the interstate natural gas pipeline industry which is directly affected by the court of appeals' decision, has a unique perspective and interest which will aid this Court in its consideration of the issues herein.

CONCLUSION

WHEREFORE, for the foregoing reasons, INGAA respectfully requests that the following brief in support of petitioners be accepted for filing.

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October 9, 1990

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TABLE OF CONTENTS

	Page
TABLE OF AUTHORITIES	ii
INTEREST OF AMICUS CURIAE	1
SUMMARY OF ARGUMENT	2
ARGUMENT	4
I. THE DECISION BELOW JEOPARDIZES THE COMMISSION'S PROGRAM TO RESTRUCTURE THE GAS INDUSTRY ALONG MORE COMPETITIVE LINES	4
II. THE DECISION BELOW UNJUSTIFIABLY EXPANDS THE FILED RATE DOCTRINE AND PREVENTS PIPELINES FROM RECOVERING THEIR COSTS	6
CONCLUSION	8

TABLE OF AUTHORITIES

Cases: Page

Associated Gas Distributors v. *FERC*, 824 F.2d 981 (D.C. Cir. 1987), *cert. denied*, 485 U.S. 1006 (1988) 4, 7

Associated Gas Distributors v. *FERC*, 893 F.2d 349 (D.C. Cir. 1989), *petitions for cert. filed*, 59 U.S.L.W. 3001 (U.S. June 20, 1990) (No. 89-1988), 59 U.S.L.W. 3001 (U.S. June 21, 1990) (Nos. 89-1989, 89-1990), 59 U.S.L.W. 3001 (U.S. June 22, 1990) (No. 89-2000), and 59 U.S.L.W. 3005 (U.S. June 21, 1990) (No. 89-2016) 2

Chevron, U.S.A., Inc. v. *Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984) 3, 7

Columbia Gas Transmission Corp. v. *FERC*, 831 F.2d 1135 (D.C. Cir. 1987), *modified on reh'g*, 844 F.2d 879 (D.C. Cir. 1988) 2

Columbia Gas Transmission Corp. v. *FERC*, 895 F.2d 791 (D.C. Cir. 1990), *petitions for cert. filed*, 59 U.S.L.W. 3005 (U.S. June 22, 1990) (No. 89-2001) and 59 U.S.L.W. 3065 (U.S. July 18, 1990) (No. 90-131) 2

FPC v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944) 7

Transwestern Pipeline Co. v. *FERC*, 897 F.2d 570 (D.C. Cir. 1990), *petitions for cert. filed*, 59 U.S.L.W. 3167 (U.S. August 24, 1990) (No. 90-344) and 59 U.S.L.W. 3167 (U.S. August 29, 1990) (No. 90-367) 2

Administrative Orders and Cases:

Order No. 500, 52 Fed. Reg. 30,334, III FERC Stats. & Regs. ¶ 30,761 (1987) 4

Transwestern Pipeline Company, 44 FERC ¶ 61,164 (1988) 7

Statutes:

Natural Gas Act, 15 U.S.C. §§ 717 *et seq.* (1988) .. 2

§ 4, 15 U.S.C. § 717c 7

TABLE OF AUTHORITIES—Continued

Page

Natural Gas Policy Act of 1978, 15 U.S.C. §§ 3301 *et seq.* (1988) 2
§ 601(c), 15 U.S.C. § 3431(c) 7

IN THE

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OCTOBER TERM, 1990

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On Petitions for Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

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BRIEF AMICUS CURIAE ON BEHALF OF THE INTERSTATE NATURAL GAS ASSOCIATION OF AMERICA IN SUPPORT OF PETITIONERS

INTEREST OF AMICUS CURIAE

The Interstate Natural Gas Association of America ("INGAA") is a non-profit national trade association representing virtually all of the major interstate natural gas transmission companies operating in the United States. The companies account for over 90 percent of all natural gas transported and sold for resale in interstate com-

merce. INGAA's members also include major Canadian interprovincial pipelines subject to regulation by the National Energy Board of Canada. INGAA's U.S. members are regulated by the Federal Energy Regulatory Commission ("Commission") under the Natural Gas Act ("NGA"), 15 U.S.C. §§ 717 *et seq.* (1988), and, to a lesser extent, under the Natural Gas Policy Act of 1978 ("NGPA"), 15 U.S.C. §§ 3301 *et seq.* (1988).

SUMMARY OF ARGUMENT

The decision below, *Transwestern Pipeline Co.* v. *FERC*, 897 F.2d 570 (D.C. Cir. 1990), is one of three cases in which the United States Court of Appeals for the District of Columbia Circuit has applied a novel and erroneous interpretation of the "filed rate doctrine" that directly contradicts this Court's prior decisions and undermines the Commission's statutory authority to prescribe "just and reasonable" rates for sales and transportation of natural gas in interstate commerce. In *Associated Gas Distributors* v. *FERC*, 893 F.2d 349 (D.C. Cir. 1989) (*"AGD II"*), *petitions for cert. filed*, 59 U.S.L.W. 3001 (U.S. June 20, 1990) (No. 89-1988), 59 U.S.L.W. 3001 (U.S. June 21, 1990) (Nos. 89-1989, 89-1990), 59 U.S.L.W. 3001 (U.S. June 22, 1990) (No. 89-2000), and 59 U.S.L.W. 3005 (U.S. June 21, 1990) (No. 89-2016), the court of appeals held that an allocation of take-or-pay costs among pipeline customers based on a "purchase deficiency" method violated the filed rate doctrine.[1] Similarly, in *Columbia Gas Transmission Corp.* v. *FERC*, 831 F.2d 1135 (D.C. Cir. 1987), *modified on reh'g*, 844 F.2d 879 (D.C. Cir. 1988) (*"Columbia I"*), and *Columbia Gas Transmission Corp.* v. *FERC*, 895 F.2d 791 (D.C. Cir. 1990) (*"Columbia II"*), *petitions for cert. filed*, 59 U.S.L.W. 3005 (U.S. June 22, 1990) (No. 89-2001) and 59 U.S.L.W. 3065 (U.S. July 18, 1990) (No. 90-131),

[1] The Commission had approved such an allocation methodology because it reasonably reflected customer responsibility for the incurrence of the allocated costs.

the court withheld the deference due the Commission by holding that an order allowing natural gas pipelines to recover through "direct bills" costs which pipelines had been required to pay producers for past sales of gas constituted unlawful retroactive ratemaking and thereby violated the filed rate doctrine. INGAA has filed as *amicus curiae* in support of petitioners in both of those proceedings.

In the instant case, the court of appeals has once again improperly applied the filed rate doctrine, and in doing so has failed to accord the Commission due deference pursuant to the standards established in *Chevron, U.S.A., Inc.* v. *Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984) (*"Chevron"*). Moreover, by expanding this Court's prior construction of the filed rate doctrine, the decision below invalidates a crucial element of the Commission's program to prevent a recurrence of the take-or-pay crisis that has severely hampered the Commission's efforts to promote competition in the interstate natural gas pipeline industry during the past decade. The Commission has concluded that to avoid future take-or-pay problems pipelines should be authorized to establish a gas inventory charge ("GIC") to handle the costs of maintaining a gas inventory responsive to customer needs. By striking down the cost recovery mechanism designed to enable pipelines to make the transition from the old ratemaking method to GICs, the decision seriously jeopardizes the Commission's entire program for dealing with future take-or-pay.

This case presents issues which are critical to the natural gas pipeline industry in making the transition to a more competitively-oriented market. In addition, the court of appeals' improper application of the filed rate doctrine in this case raises issues similar to those addressed by the Commission in its petitions for writ of certiorari in *AGD II* and *Columbia II*. INGAA therefore recommends that certiorari be granted herein.

ARGUMENT

I. THE DECISION BELOW JEOPARDIZES THE COMMISSION'S PROGRAM TO RESTRUCTURE THE GAS INDUSTRY ALONG MORE COMPETITIVE LINES

The central barrier to the Commission's effort during the 1980's to reshape the natural gas industry and promote competition in gas supply markets has been the system of take-or-pay contracts entered into by pipelines and producers during the prior decades. As recognized by the court of appeals in *Associated Gas Distributors* v. *FERC*, 824 F.2d 981 (D.C. Cir. 1987), *cert. denied*, 485 U.S. 1006 (1988) ("*AGD I*"), the Commission could not reasonably adopt one of the key elements of this restructuring—the open-access, non-discriminatory transportation program—without also addressing the issues created by these take-or-pay contracts. The Commission's answer in Order No. 500 was essentially two-pronged. As to the costs of settling *past* take-or-pay disputes or amending uneconomic contracts, the Commission adopted the so-called "equitable sharing" plan at issue in *AGD II*. The Commission addressed future take-or-pay by authorizing pipelines to establish a rate mechanism that would prevent a repetition of the crippling build-up of take-or-pay costs that plagued the industry under the prior system. The mechanism—a "gas inventory charge"—was specifically designed to "help pipelines restructure their service obligations to customers and their purchase obligations to producers so as to reflect the realities of anticipated future operations and prevent future take-or-pay problems." Order No. 500, 52 Fed. Reg. 30,334 at 30,346, III FERC Stats. & Regs. ¶ 30,761 at 30,793 (1987).

In practical effect, GICs, such as the one granted Transwestern Pipeline Company ("Transwestern"), were intended to replace the traditional purchased gas adjustment ("PGA") cost recovery mechanism by compensating

pipelines for standing ready to provide sales services to the extent of customer nominations.[2] To the extent a customer does not take the volumes it nominates, it pays an inventory charge. This is the pipeline's compensation for its gas supply service.

A number of pipeline applications have been filed with the Commission to implement GICs and eliminate the pipelines' PGA clauses. A necessary element of any such GIC is a means to recover the remaining balance of unrecovered gas costs at the time the PGA is terminated and the GIC takes effect. As noted by the Commission in its petition for writ of certiorari herein, the decision below precludes recovery of these remaining balances and may deter pipelines from instituting gas inventory charges. This will thwart the Commission's policy of avoiding future take-or-pay problems and encouraging competition. Petition at 9-10.

The plain fact is that a pipeline is highly unlikely to institute a gas inventory charge if the price of doing so is to preclude recovery of substantial unrecovered purchased gas costs.[3] It is not feasible for a pipeline to institute a new gas pricing mechanism keyed to competitive

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[2] Transwestern's PGA was a cost recovery mechanism similar to one that has been widely used by regulated interstate pipelines with the approval of the Commission. PGAs were instituted in 1972 when pipelines served as the primary merchants of natural gas, and when, for the most part, gas producers sold directly to pipelines, and pipelines subsequently resold the gas. PGA cost recovery mechanisms were designed to enable pipelines to manage their gas acquisition programs without having to file new rate cases in response to frequent variations in gas costs. Thus, any pipeline with a PGA provision in its tariff could defer to Account No. 191 any over- or undercollections of actual purchased gas costs. It is the court of appeals' denial of recovery of these Account No. 191 amounts by direct billing that is at issue here.

[3] The magnitude of such costs varies by pipeline, of course, but INGAA is aware of Account No. 191 balances of nearly $200 million on a single pipeline.

gas markets if it is forced to absorb prudently incurred costs in meeting its certificated sales service obligations. To the extent that pipelines are forced to absorb such costs, it will undercut the pipelines' merchant function, and prevent them from having a meaningful role in the gas sales market. The Commission's determination that pipelines may directly bill costs deferred to Account No. 191 is thus a vital step in the industry's transition process. It authorizes a just and reasonable—and lawful—rate methodology that suits the industry's current circumstances and properly assigns costs to customers who were responsible for their incurrence.

II. THE DECISION BELOW UNJUSTIFIABLY EXPANDS THE FILED RATE DOCTRINE AND PREVENTS PIPELINES FROM RECOVERING THEIR COSTS

When Transwestern filed for authority to bill the costs at issue directly it proposed no change in rates that would implicate the filed rate doctrine. Instead, it merely sought to alter the *mechanism* for recovery of purchased gas costs which were properly included in Account No. 191. Had Transwestern simply continued its purchased gas adjustment provision, such costs would have been collected in the normal course of events. Although the Account No. 191 costs at issue arose from past purchases, the proposed direct bill in no way altered the rates associated with past purchases. The decision below therefore is premised on a fundamental, but erroneous, assumption: that a direct bill to eliminate the remaining Account No. 191 balance transforms otherwise proper charges into retroactive rates. In the court of appeals' view, because the cost recovery mechanism changed—from the PGA surcharge to a direct bill—Transwestern should be denied recovery of purchased gas costs which were incurred on behalf of Transwestern's sales cus-

tomers and for which there has been no claim of imprudent action.[4]

The court of appeals' decision, if affirmed, will deny pipelines the reasonable opportunity to recover prudently incurred costs to which they are statutorily entitled. The result of the decision below, therefore, is directly at odds with this Court's clear guidance in *FPC* v. *Hope Natural Gas Co.*, 320 U.S. 591 (1944) (*"Hope"*). Moreover, the court's decision defies the rule of *Chevron*, *supra*, concerning statutory construction and the deference due an agency interpreting its organic statute. Because the costs at issue were prudently incurred, and because the "end-result" reached by the Commission was the product of a "permissible" interpretation of the authority vested under Section 4 of the NGA, the Commission must be sustained. *See Hope* and *Chevron*, *supra*. Finally, further support for upholding the Commission is found in Section 601(c) of the NGPA, 15 U.S.C. § 3431(c) (1988), which guarantees, absent fraud, abuse, or similar grounds, that pipelines may pass through any amounts paid with respect to any purchase of natural gas. The reality is that the court of appeals' decision would make fair and compensatory cost recovery a practical impossibility given the transformation in natural gas markets over the last decade. *See AGD I*, 824 F.2d at 1025-1026.

INGAA submits that certiorari should be granted in this proceeding for the same reasons set forth in INGAA's brief *amicus curiae* in *AGD II* and *Columbia II*: that is, the D.C. Circuit has incorrectly and unjustifiably expanded the filed rate doctrine as well as the rule against

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[4] In authorizing Transwestern's direct billing, the Commission stated that "[t]o require Transwestern to absorb potential under-collections related to gas purchases made before implementation of the GIC would be unreasonable because there is no showing that the costs at issue have been imprudently or abusively incurred." *Transwestern Pipeline Company*, 44 FERC ¶ 61,164 at 61,537 (1988).

retroactive ratemaking and has thereby improperly limited the Commission's ratemaking authority by substituting its judgment for that of the Commission. As noted by the Commission and Transwestern in their respective petitions for certiorari herein, the D.C. Circuit in this case followed essentially the same analytical approach as it did in *AGD II* and the *Columbia* decisions.

CONCLUSION

For the foregoing reasons, the petitions for writ of certiorari should be granted.

Respectfully submitted,

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October 9, 1990

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